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PART B

BUDGET BRIEFING 1984

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PART B



9 MAR 1984



FROM: J O KERR  
DATE: 9 March 1984

Mr Monger

cc Chief Secretary  
Economic Secretary  
Financial Secretary  
Minister of State  
Sir P Middleton  
Mr Cassell  
Mr Battishill  
Mr Watson  
Mr Allen  
Mr G P Smith

Mr Mace: IR

F  
BUDGET: CONTACTS WITH DHSS J

The Chancellor has seen your minute of 6 March, and is content that you should maintain the procedure followed in previous years, and mention the Budget changes to income tax rates and allowances to a very small group of DHSS officials on a totally personal and restricted basis. He is clear that the DHSS officials must be told of nothing apart from income tax rates and allowances.

J O KERR



Ch/Ex Ref No

B.(84).567



FROM: MISS M O'MARA

DATE: 9 March 1984

PS/Financial Secretary

cc PS/Chief Secretary  
 PS/Minister of State  
 PS/Economic Secretary  
 Mr Kemp  
 Mr Ridley  
 Mr Lord  
 Mr Portillo  
 PS/Inland Revenue  
 Mr Driscoll/IR  
 Mr Graham (Parl Counsel)

MPs' EXPENSES PAYMENTS AND TAX: TIMING OF LEGISLATION

This is to confirm the Chancellor's comments on your minute of 8 March which I passed to you yesterday evening.

2. The Chancellor wishes to table the Resolution on Budget Day in its short form. He would like the Inland Revenue to issue a Press Release at the same time and has asked that the Financial Secretary should send this under cover of a personal letter to all Members. He sees no need to mention the measure in any speech during the Budget Debates, although he would not object if the Financial Secretary wished to include a passage. He sees no need to publish the clause in advance of its appearance in the Finance Bill itself.

A handwritten signature in cursive script, appearing to read 'MOM'.

MISS M O'MARA



CH/EX REF. NO. B(84) 550

FROM: MISS M O'MARA

DATE: 9 March 1984

cc Chief Secretary  
Financial Secretary  
Minister of State  
Economic Secretary  
Mr Battishill (*without attachment*)  
Mr Evans  
Mr Lavelle  
Mr Botrill  
Mr Shields  
Mr Odling-Smee  
Mr Ridley  
Mr Lord

MR FOLGER (WITHOUT ATTACHMENT)

**BUDGET SPEECH: THE ECONOMIC BACKGROUND**

I should be grateful if you would co-ordinate comments from copy recipients on this section of the speech and let me have any suggested amendments by lunch time today.

*MOM*

MISS M O'MARA



**THE ECONOMIC BACKGROUND**

8. But I start with the economic background, and the convincing evidence of recovery: a recovery that springs from the monetary and fiscal policies to which we shall hold.

9. Since 1980, inflation has fallen steadily from a peak of over 20 per cent. Last year it was down to about 4½ per cent, the lowest figure since the sixties. And with lower inflation have come lower interest rates.

10. The underlying strength of the recovery is clear. Whereas in some previous cycles recovery has come from a self-defeating stimulus to monetary demand, this time its roots are in our commitment to sound finance and honest money. Lower inflation and lower interest rates benefit industry, business, and consumer confidence. Falling inflation has made room for real growth, as we always said it would.

11. 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 ~~clearly~~ 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.



12. 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 during 1983 manufacturing productivity grew by 6 per cent with no sign of slowing down. 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.

13. Higher profits lead to more jobs. The number of people in employment increased by about 85,000 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. This is encouraging news for the unemployed and those who will be leaving school this summer.

14. But further progress ~~on productivity~~ is needed: although our unit wage costs in manufacturing rose by under 3 per cent last year, such costs actually fell in the US, Japan and Germany, our three biggest competitors. The employment prospect would be significantly improved if a bigger contribution to improved <sup>competitiveness</sup> ~~productivity~~ were to come from lower pay rises. Good sense about pay remains vital.

15. 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.

16. Imports rose a little faster than home demand last year, as the UK emerged from recession ahead of our main trading partners - our rate of economic growth last year was the highest in the European Community. For much of 1983 our export performance reflected the weakness in many of our overseas markets. 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.

17. Our critics have been confounded by the combination of recovery and low inflation. Even the pessimists have been forced to acknowledge the strength 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, personal consumption will continue to grow. And the recovery is already becoming more broadly based. Encouraged by improved profitability and better long-term growth prospects, investment is expected to rise by 6 per cent this year.



18. Looking abroad, economic prospects are also more favourable than 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.

19. Of course, there are inevitable risks and uncertainties. The size and continued growth of the United States budget deficit causes widespread concern, not least among Americans, and keeps American, and hence international, interest rates high. This acts as a brake on world recovery and worsens the problems of the debtor countries. Another consequence is a massive and still growing deficit in the US current balance of payments, financed by inflows of foreign capital, and leading to mounting pressures for protectionism within the United States, and sharp exchange rate movements. It is an unstable situation, creating worrying uncertainties.

20. A second potential risk is disruption in the oil market. The immediate prospects are less obviously volatile than they were a year ago. But uncertainties remain, and the United Kingdom, and indeed the world economy, inevitably remains vulnerable to any major disturbances.

21. But despite these risks there is a growing sense throughout the industrialised world that the recovery this time is not merely cyclical, but one which can be sustained. The essential requirement is the continued pursuit of prudent monetary and fiscal policies.



CH/EX REF. NO. BC8A/574.

FROM: J O KERR

DATE: 9 March 1984

cc PS/Chief Secretary  
PS/Financial Secretary  
PS/Minister of State  
PS/Economic Secretary  
Sir P Middleton  
Mr Cassell  
Mr Monck  
Mr Monger  
Mr Battishill  
Mr Griffiths  
Mr Ridley  
Mr Lord  
Mr Portillo  
PS/C&E

MR JEFFERSON SMITH - CUSTOMS AND EXCISE

**VAT ON IMPORTS**

The Chancellor has seen your minute of 7 March, and the Minister of State's comments, as recorded in Mr Corcoran's of 8 March.

2. On the question of the quotability of the legal advice, he is inclined to think that it will be sufficient at the outset to rest on the statement that the continuation of postponed accounting for raw materials is not feasible because it would be unlawful. If the pressure grows to the extent that it becomes essential to be able to attribute this view to the Law Officers, he would then be prepared to approach the Attorney General, invoking the last sentence of the letter of 7 March from the Lord Advocates' Chambers.

A handwritten signature in black ink, appearing to be 'J O Kerr'.

J O KERR



CH/EX REF. NO. B 84 557

FROM: MISS M O'MARA

DATE: 9 March 1984

cc Chief Secretary  
Financial Secretary  
Minister of State  
Economic Secretary  
Mr Folger (*without attachment*)  
Mr Odling-Smee  
Mr Ridley  
Mr Lord  
PS/IR

MR BATTISHILL (WITHOUT ATTACHMENT)

**BUDGET SPEECH: INTRODUCTION**

I should be grateful if you would co-ordinate comments from copy recipients on this section of the speech and let me have any suggested amendments by lunch time today.

*MOM*

MISS M O'MARA



**INTRODUCTION**

This Budget will set the Government's course for this Parliament. It is founded on the policies which we have consistently followed since 1979.

2. Consistency of purpose is the hallmark of this Government. It is the only way to improve economic performance and lay the foundations for future prosperity, more jobs and lower taxation. Above all, it is the only way to defeat inflation and achieve our ultimate objective of stable prices.

3. The results of the Medium Term Financial Strategy introduced in 1980 can be seen in four years of falling inflation, down now to the lowest levels since the sixties. And that in turn has brought a steady recovery of output, rising living standards and, more recently, rising employment.

4. The facts speak for themselves. They are a tribute to the courage and foresight of the five Budgets presented from this Despatch Box by my distinguished predecessor, the present Foreign Secretary, whose duties sadly keep him in Brussels today.

5. Today's Budget has two themes: first, the further reduction of inflation, which will further improve the prospects



for jobs; and second, the reform and simplification of the tax system, ~~which will make it fairer for all.~~

6. 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. Some of these cuts I shall announce today, for this is in a sense a Budget for two years. In a wider sense it is a tax reform Budget, setting out a tax strategy for this Parliament.

7. As usual, a number of press releases will be issued today, filling out the details of my tax proposals.





FROM: MISS M O'MARA

DATE: 9 March 1984

cc Chief Secretary  
Financial Secretary  
Minister of State  
Economic Secretary  
Mr Battishill (*under attachment*)  
Mr Cassell  
Mr Odling-Smee  
Mr Ridley  
Mr Lord  
PS/IR

MR MONGER

**BUDGET SPEECH: TAX REFORM**

I should be grateful if you would co-ordinate comments from copy recipients on this section of the speech and let me have any suggested amendments by lunch time today.

*Mom*

MISS M O'MARA



## TAX REFORM

58. I mentioned 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 indeed over the whole MTFPS period - ] and I hope to have scope for further reductions in tax in subsequent Budgets.

59. 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.

60. 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, if I may borrow a phrase from the Rt Hon member for Leeds East, the howls of anguish from the latter group tend to be rather more audible than the murmurings of satisfaction from the former.

61. ~~Reform must succeed, but need not be, in this sense, a howling success.~~ So I have rejected the extreme suggestion, popular in some quarters, that I should scrap our income-based tax system and replace it with a brand new expenditure-based system. A reform of this kind would produce, in the real world, an upheaval of mind-boggling dimensions.



62. But I don't believe we can afford to opt for the quiet life and do nothing. So I have chosen the middle way: to work for improvements, some I believe very substantial, but 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.

63. 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.



CH/EX REF. NO. EG/559

FROM: MISS M O'MARA

DATE: 9 March 1984

cc Chief Secretary  
Financial SecretaryEconomic Secretary  
Mr Battishill (*without attachment*)  
Mr Cassell  
Mr Lankester  
Mr Odling-Smee  
Mr Ridley  
Mr Lord  
PS/IR

MR MONGER

**BUDGET SPEECH: SAVINGS AND INVESTMENT**

I should be grateful if you would co-ordinate comments from copy recipients on this section of the speech and let me have any suggested amendments by lunch time today.

*MOM*

MISS M O'MARA



## SAVINGS AND INVESTMENT

64. First, the taxation of savings and investment. The proposals I am about to make should improve both 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 intermediary institutions.

65. First, stamp duty. This was doubled from its long-standing 1 per cent by the post-war Labour Government in 1947, reduced by the Macmillan Government in 1963, and once again doubled to 2 per cent in the first Budget presented by the Rt Hon member for Leeds East in 1974. At its present level it is an impediment to mobility and incompatible with the welcome movement to greater competition in the City, following the withdrawal of the Stock Exchange case from the Restrictive Practices Court.

66. I therefore propose to halve the rate of stamp duty to 1 per cent. [Transactions from today will benefit from the new rate, unless documents have to be stamped before 20 March, which is the earliest date on which the change will have legal effect.]

67. For the home buyer, the new flat rate 1 per cent stamp duty will start at <sup>(an increase threshold of)</sup> £30,000. Below this level no duty will in future be payable, and 90 per cent of first time home buyers will therefore not be liable for stamp duty at all.



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

X  
69. In addition, I have three 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 convertible loan stock which were announced but not enacted last year. And I propose to exempt from Capital Gains Tax certain corporate fixed interest securities provided they are held for more than a year. Since such securities are already exempt from stamp duty ~~an exemption I can confirm also extends to certain convertible loan stocks~~ this means that the tax concessions for Government borrowing in the gilt-edged market will now be virtually the same as for private sector borrowing in the corporate bond market.

X

70. 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 real estate.

71. Next, life assurance. I have concluded that there is no longer any justification for Premium Relief on Life Assurance,



which is now only one of a number of savings channels for ordinary people. The main effect of the relief today is to encourage institutional rather than direct investment, and to spawn a multiplicity of well-advertised tax management schemes. I propose to withdraw the relief on all new policies made after today. I stress that this change will apply only to new (or newly enhanced) policies, taken out or increased after today. Existing policies will not be affected at all. The change is estimated to yield £90 million in 1984-85.

72. We must also review unjustified penalties on 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 businessman 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 in the first place 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 more than half would otherwise be liable to tax at only the basic rate.

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

74. 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.

75. One inequality 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.

76. But the major inequality of treatment, against which the banks in particular have frequently complained, lies with the special arrangement for interest paid by building societies, under which 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.

77. 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 suffer the deduction of tax at the composite rate. However, it is always open to such depositors to put their savings elsewhere, such as National Savings. 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 are spared the need to recruit an additional 2000 staff to collect the tax due on interest paid without deduction.



78. 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.

79. Non-taxpayers would ~~of course~~ 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. Moreover I have decided to reduce substantially the permitted maximum size of future holdings in the National Savings Investment Account and in Income Bonds.

80. The true purpose of the move is simple: simplicity itself. Unless they are higher rate taxpayers, 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 be deducted at source. The Inland Revenue will be able to make staff savings of up to an extra 1000 civil servants. Moreover, this figure takes no account of the extra numbers that would have



been required to operate the present system as the trend towards the payment of interest on current accounts develops.

81. Accordingly, I propose to extend the composite rate arrangements to interest received by UK 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.

82. Taken together, the major proposals I have just announced on stamp duty, life assurance 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. And they will reinforce the Government's policy of encouraging competition in the financial sector, as in the economy as a whole.



CH/EX REF. NO. B(84) 560



FROM: MISS M O'MARA

DATE: 9 March 1984

- cc Economic Secretary
- Mr Cassell
- Mr Battishill (*writes letter sheet*)
- Mr Evans
- Mr Odling-Smee
- Mrs Lomax
- Mr Ridley
- Mr Lord

MR LANKESTER

**BUDGET SPEECH: PUBLIC SECTOR BORROWING ETC**

I should be grateful if you would co-ordinate comments from copy recipients on this section of the speech and let me have any suggested amendments by lunch time today.

*Mom*

MISS M O'MARA



BUDGET SECRET

PUBLIC SECTOR BORROWING ETC

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

40. The MTFSS has always envisaged that the Public Sector Borrowing Requirement would fall as a percentage of Gross Domestic Product over the medium term. And it has, notably as a result of the courageous Budget introduced by my predecessor in 1981, which brought the PSBR down to 3½ per cent of GDP in 1981-82.

41. Since then 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 3½ per cent of GDP. This is significantly above what was intended at the time of last year's Budget, and would of course have been higher still had it not been for the measures taken last July.

42. 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 and so by the US situation which I have already described: but that makes it all the more



BUDGET SECRET

important to curb domestic pressures. In contrast to virtually the whole of the post-war period, UK longer-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.

43. The higher level of asset sales planned 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 is less than the effect of direct ~~cuts~~<sup>reductions</sup> in Government spending programmes.

44. Last year's MTFS showed an illustrative PSBR for 1984-85 of 2½ 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 have therefore decided to provide for a PSBR next year of 2¼ per cent of GDP, or roughly £7 billion.

45. 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, [coupled with the decisions taken in the Public Expenditure Survey and the continuing effects of the July measures,] have changed the picture. Bringing the PSBR down to £7 billion will not



BUDGET SECRET

require such an increase in taxation. In fact it will require no overall net increase at all. So the measures I shall shortly announce will, after indexation, be broadly neutral in their effects on revenue in 1984-85.

46. Better still, they will reduce taxation in 1985-86 by some £1½ billion. And the MTFs published today shows that there should be room <sup>for</sup> further tax cuts not only in 1985-86, but throughout the remainder of this Parliament, provided ~~if~~ ~~that~~ that we stick firmly to our published plans for public expenditure to 1986-87, and maintain an equally firm control of public spending thereafter.





FROM: MISS M O'MARA

DATE: 9 March 1984

cc Economic Secretary  
Mr Cassell  
Mr Battishill (*with attachment*)  
Mr Evans  
Mr Odling-Smee  
Mrs Lomax  
Mr Ridley  
Mr Lord

MR LANKESTER

**BUDGET SPEECH: THE MTFs**

I should be grateful if you would co-ordinate comments from copy recipients on this section of the speech and let me have any suggested amendments by lunch time today.

*Mon*

MISS M O'MARA



**THE MTFS**

22. 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 been driven to stagger from one short-term policy expedient to another. The temptation to accommodate inflationary pressures proved irresistible, and the nation's longer-term economic performance was progressively undermined.

X 23. The discipline of the MTFS was designed to 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.

24. People now know that the Government intends to stick to its medium term objectives. They understand that the faster inflation comes down, the faster output and employment recover. Increasing realism, and flexibility in the economy, owes much to the pursuit of firm and consistent policies within the MTFS framework.



25. Originally the MTFS covered four years. In this first Budget of a new Parliament we have thought 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 last two years of the new MTFS, which lie beyond the period covered in last years Public Expenditure Survey and last month's White Paper, the Government has not yet made firm plans for public spending. But the MTFS assumption - and 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.

26. The precise figures set out in the MTFS are not of course a rigid framework, lacking all flexibility. As in the past, there may well need to be adjustments to take account of changing circumstances. But such changes will be made only when they will not jeopardise the consistent pursuit of the Government's objectives.



CH/EX REF. NO. B(24)562

FROM: MISS M O'MARA

DATE: 9 March 1984

cc Economic Secretary  
Mr Cassell  
Mr Battishill (without attachment)  
Mr Evans  
Mr Odling-Smee  
Mrs Lomax  
Mr Ridley  
Mr Lord

MR LANKESTER

**BUDGET SPEECH: MONETARY POLICY**

I should be grateful if you would co-ordinate comments from copy recipients on this section of the speech and let me have any suggested amendments by lunch time today.

*MOM*  
MISS M O'MARA



## MONETARY POLICY

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

28. Over the twelve months to mid-February the growth of M3 has been well within the 7-11 per cent target range, with M1 and PSL2 at or a little above the top of it. While in the early months of the target period most measures of money showed signs of accelerating, growth in all the target aggregates has since the summer been comfortably within the range.

29. Other evidence confirms that monetary conditions are satisfactory. The effective exchange rate has remained fairly stable, despite the international uncertainties and instability which I have described. And nominal interest rates have continued to decline in line with falling inflation.

30. To maintain sound monetary conditions in the years ahead the monetary targets must reflect changes in the financial system and in the significance of different measures of money. There is nothing new in this. Over the years we have altered the target ranges and aggregates to take account of such changes. But the thrust of the strategy has been maintained.



31. One important development has been the attempt to give a more explicit role to the narrow measures of money. Even when targets were set solely in terms of £M3, we recognised the significance of their behaviour. £M3 and the other broad aggregates give a good indication of the growth of liquidity. But a large proportion of this money is deposited in ways which earn interest. In defining policy it is therefore helpful also to make specific reference to measures of money which bear very little interest, and provide a good guide to the immediate potential for spending.

32. M1 was for this reason introduced as a target aggregate, but it has not proved entirely satisfactory for that purpose. Its behaviour has been dominated by changes in its large interest-bearing component, which has grown rapidly, and now accounts for 25 per cent of the total. With the introduction of new, interest bearing chequing accounts, the signs are that this will continue.

33. Other measures of narrow money have not been distorted to the same extent. In particular, M0, which consists mainly of currency, has not been subject to this development. It has been affected by other innovations that have reduced people's need for cash, but the pace of change has not diminished its value as an indicator of financial conditions. There is also the new aggregate M2, which was specifically devised to provide a comprehensive measure of transactions balances and which may in time prove a useful guide, but still needs to be interpreted with particular care.



34. 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 to grow more slowly than broader measures. And this year's Red Book sets out two separate ranges.

35. The target range for broad money will continue to apply to £M3, and for the coming year will be set at 6-10 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 4-8 per cent. To avoid any possible misunderstanding, I stress that the use of MO as a target aggregate will not involve any change in methods of monetary control.

36. Both target ranges will have equal importance in formulating policy. And we shall continue to take into account other measures of money, especially M2 and PSL2, as well as wider evidence of financial conditions, including the exchange rate. As in the past, we shall seek to influence monetary conditions by an appropriate combination of funding and operations in the money market.

37. So far as funding is concerned, the role of the National Savings movement will remain important. This year's target of £3 billion is likely to be achieved: the target for the coming year will again be £3 billion.

38. 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.



CH/EX REF. NO. BBU 563.

FROM: MISS M O'MARA

DATE: 9 March 1984

cc Chief Secretary *M Bailey*  
Mr Anson  
Mr Battishill (without attachment)  
Mr Odling-Smee  
Mr Pestell  
Mr Watson  
Mr Ridley  
Mr Lord

MR SCHOLAR

**BUDGET SPEECH: PUBLIC EXPENDITURE**

I should be grateful if you would co-ordinate comments from copy recipients on this section of the speech and let me have any suggested amendments by lunch time today.

*mom*

MISS M O'MARA



BUDGET SECRET

PUBLIC EXPENDITURE

47. 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 critically important issue of government spending in a rather wider perspective.

48. For far too long, spending has grown faster than has the economy as a whole. The trend has seemed inexorable, and the result has been that the great mass of the population have had to pay more and more in tax. To take just one example: as recently as 1963-64 no married man had to pay a penny of income tax unless his taxable income was at least 45 per cent of the average earnings level. Today the tax threshold is down to ~~little more than~~ under a third of average earnings. Over the years more and more people on lower and lower incomes have been brought into income tax.

49. We have seen a steady enlargement in the role of the State, at the expense of the individual, and a steady increase in the dead weight of taxation dragging down our economic performance as a nation.

50. Clearly this ~~dangerous~~ process has to stop. Of course, much public spending is directed to eminently desirable ends. But there is an important choice to be made; and it is not



BUDGET SECRET

enough simply to make marginal changes in spending programmes from year to year. The choice needs more fundamental national consideration and debate; and it needs to be set within a longer time horizon.

51. I am therefore publishing today, in addition to the customary Budget documents, a Green Paper on the prospects for public spending and taxation in the next ten years. It examines past trends; discusses pressures for still higher spending; and examines the rewards for the individual if these pressures can be contained.

52. 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 spending does not rise in real terms over the next ten years. If, on the other hand, spending grows by 1 per cent a year in real terms after 1988-89, the tax burden would by 1993 be only just below the 1978-79 level, and still well above its level in the 1960s, even if the economy grows by about 2 per cent a year over the ten years. And of course excessive taxation slows the whole economy.

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



BUDGET SECRET

It is a discussion document - descriptive not prescriptive - and we shall welcome the fullest possible discussion.

54. I can at once inform the House of a further innovation. In contrast to previous years, I have no specific public expenditure measures to announce in this Budget. The White Paper plans stand.

55. But lest the innovation seems too sweeping, I can make one small announcement, which I think the House will welcome. Within the plans we have been able to provide the National Heritage Memorial Fund with additional resources which will enable them among other things to secure the future of Calke Abbey. My Rt Hon Friend the Secretary of State for the Environment is providing £6.3 million from his planned expenditure for this year and next, and I have accepted a claim on the Reserve of £2 million for next year.

56. The House will recall that the proposals for the new rates of social security benefit to come into force in November are not now made on Budget day. 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. Accordingly, my Rt Hon Friend the Secretary of State for Social Services will be announcing the new rates of social security benefits, including Child Benefit, in June.



BUDGET SECRET

57. Before turning from Government spending to Government revenue, I should add a word on public sector manpower. At the beginning of the last Parliament, the Government set itself 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 has been achieved. We have now set ourselves the further target of 593,000 by April 1988, and I am confident that it too will be achieved, and that a leaner Civil Service will continue to operate with increasing efficiency. Speaking for my own Departments, the tax changes I shall be announcing today will reduce manpower requirements by at least 1000 which will help towards meeting the 1988 target.



CH/EX REF. NO. BL 84/564.

FROM: MISS M O'MARA

DATE: 9 March 1984

cc Chief Secretary  
Financial Secretary  
Minister of State  
Economic Secretary  
Mr Cassell  
Mr Battishill (without attachment)  
Mr Odling-Smee  
Mr Ridley  
Mr Lord  
PS/IR

MR MONGER

**BUDGET SPEECH: PERSONAL TAXATION**

I should be grateful if you would co-ordinate comments from copy recipients on this section of the speech and let me have any suggested amendments by lunch time today.

*MOM*

MISS M O'MARA



**PERSONAL TAXATION**

151. 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.

152. During the lifetime of this Parliament, I intend to carry much further 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 make a start now.

153. 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.



154. I have decided that, this year, the right course is to use every penny I have in hand, within the framework of a revenue neutral Budget, to lift the level of the basic tax thresholds, for the married and single alike. It is fundamentally wrong that we collect income tax from people whose incomes are so low that they are entitled to social security benefits on grounds of need. Moreover low tax thresholds make the poverty and unemployment traps much worse, so that the financial incentive to find a better job or even any job may decline almost to zero. There is, alas, no quick or cheap solution to these problems. But that is all the more reason to make a start on solving them now.

155. I propose to increase most thresholds in line with the statutory requirement, and 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 of £38,100 or more. The single age allowance will rise from £2,360 to £2,490 and the married age allowance from £3,755 to £3,955.

156. 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 person's threshold will be increased by £220, from £1,785 to £2,005; and the married threshold by £360, from £2,795 to £3,155. ~~The special allowances for widows, and for single parents, will as a consequence go up by some 14 per cent.~~



157. This is an increase of around 12½ per cent, or some 7 per cent in real terms. It brings the married man's tax threshold for 1984-85 to its highest level in real terms since the war. It means that every tax-paying married couple in the land 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. ~~And~~ Some 850,000 people - over 100,000 of them widows - will not pay tax in 1984-85 who would have paid if thresholds had not been increased. And 400,000 fewer than if the allowances had merely been indexed.

158. 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.

159. This is as far as I can go on income tax this year, within a broadly revenue-neutral Budget for 1984-85. But as I have already said, so long as we hold to our published planned levels of public spending, there is an excellent prospect consistent with the necessary downward path of public borrowing of further tax cuts 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 some £1½ billion, with business taking the lion's share. So for next year I would hope to be concentrating on further help to individuals, and principally on income tax.



## CONCLUSION

160. I have, Mr Deputy Speaker, completed the course I charted at the outset this afternoon. I have described the recovery, and how the Government plans to sustain it, by working for further reductions in inflation, by maintaining sound money and by curbing borrowing. I have described a three part reform strategy for a fairer, simpler tax system. And I have been able to propose substantial tax reductions over two years in a Budget that is revenue-neutral for 1984-85. It is a Budget for responsibility and reform; and I commend it to the House.

W-20



19

CH/EX REF. NO. B(84)585

FROM: MISS M O'MARA

DATE: 9 March 1984

cc Chief Secretary  
Financial Secretary  
Mr Cassell  
Mr Lovell  
Mr Odling-Smee  
Mr Ridley  
Mr Lord  
PS/IR

MR MONCK

**BUDGET SPEECH: BUSINESS TAXATION**

I should be grateful if you would co-ordinate comments from copy recipients on this section of the speech and let me have any suggested amendments by lunch time today.

*mom*

MISS M O'MARA



## BUSINESS TAXATION

83. I now turn to company taxation.

84. In this area, Government has 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.

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

86. 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 investment decisions and choices about finance. Others were introduced to meet short-term pressures, notably the upward surge of inflation. With inflation down to 5 per cent and set to go lower, 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 unprofitable investment at the expense of jobs.

87. 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.

88. 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 (though not commercial) buildings. But there is little evidence that these incentives have strengthened the economy or improved the quality of investment. 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.

89. The nation needs more investment, and the 6 per cent increase forecast for this year is encouraging. But the greatest benefits flow from investment decisions based on analysis of future market assessments, not future tax assessments.

90. 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.

91. 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 in advance of their being brought into use.

92. 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. I should add that, when these changes have all taken place, in respect of both plant and machinery and industrial buildings, tax allowances will still on average be rather more generous than would be provided by a strict system of economic depreciation.

93. The changes in the rates of allowances will not apply to payments under binding contracts entered into on or before today, provided that the expenditure is incurred within the



next three years.

94. After consulting my Rt Hon Friend the Secretary of State for Trade and Industry, I have decided to make transitional tax arrangements for certain investment projects in the regions. Existing capital allowances will continue to apply to expenditure on projects in Development Areas and special Development Areas for which regional development grants are available and offers of selective assistance have already been made between 1 April 1980 and today. Similar arrangements were announced for regional development grants in my Rt Hon Friend's White Paper on Regional Industrial Development last December.

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

96. Next, stock relief. As the House will recall, this was introduced by the last Labour Government as a rough and ready form of emergency help to businesses facing the ravages of high inflation. These days are past; and relief is no longer necessary; for company liquidity has improved and, above all, inflation has fallen sharply, ~~and will be falling further during this Parliament.~~ Accordingly, I propose to abolish stock relief from this month.



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

98. All these rates for the years ahead will be included in this year's Finance Bill.

99. And they will bring a further benefit. Responses to the Corporation Tax Green Paper published in 1982 revealed a strong and general desire to retain our imputation system of Corporation Tax. This allows a company to offset in full all interest paid. But only a partial deduction for dividends is allowed. Companies thus have an unhealthy incentive to finance themselves through borrowing, 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.

100. 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.

101. The Corporation Tax measures I have just announced will cost £280 million in 1984-85. In 1985-86 the cost will be £600 million - made up of £1,150 million by way of reductions in the rates, only partially offset by a £550 million reduction in the value of the reliefs. The estimated costs for later years, which have been provided for in the MTF5 figures contained in the Budget Red Book, have been drawn up on a cautious basis. Thus business and industry can go ahead confidently on the basis of the Corporation Tax rates I have announced today, and which set the framework of company taxation for the rest of this Parliament.

102. I expect these changes to have both a somewhat different impact in the short and long term. In the short term, some investment should be forward over the next two years, to take advantage of high first year capital allowances while they last - a prospect made all the more alluring for business by virtue of the fact that profits earned will be taxed at the new lower, rates. But the more important and durable effect will be to encourage the search for investment projects with a genuinely worthwhile return, and to discourage uneconomic investment.

103. It is doubtful if it was ever really sensible to subsidise capital irrespective of the true rate of return. Certainly,



with over three million unemployed it cannot make sense to do so.

104. 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 net profits should encourage and reward enterprise and stimulate [higher current expenditure and ] innovation in all its forms - research and development and work on new products, processes and markets. They are the centre-piece, for business, of this Budget and the tax strategy for this Parliament.

105. But I have further measures to announce that are relevant to business.

106. First, 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.

107. The scheme was designed to offer generous incentives for investment in high risk areas by new or expanding companies. Farming is clearly not an area which falls within this category, and I therefore propose that from today farming should cease to be treated as a qualifying trade under the scheme. I am



also ready to consider tightening the scheme further, if it becomes clear at any time in the future that it is being used for purposes for which it was clearly not designed.

108. Secondly, as a measure of help to small firms, I propose to raise the VAT registration threshold with effect from midnight tonight from £18,000 to £18,700.

109. Thirdly, in keeping with what I have said about removing 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.

110. The first distortion is the 50 per cent <sup>tax</sup> deduction (falling after 9 years to 25 per cent) <sup>applied to</sup> ~~given from~~ the emoluments of foreign employees working here for foreign employers. Foreign employees are often paying much less tax here than they would either at home or in most other European countries. At present income tax rates, the need for the relief has clearly disappeared. Moreover it is open to widespread abuse. It is, for example, possible for the son of an immigrant, working here for a foreign company, to pay tax on only 75 per cent of his salary, even if he himself has lived in this country all his life. I therefore propose to withdraw the relief entirely for all new cases from today, and to withdraw the 25 per cent deduction from existing beneficiaries from 6 April next. The 50 per cent deduction will be phased out over the



5 years to 5 April 1989.

111. I also propose to withdraw the so-called foreign earnings relief for United Kingdom residents who perform their duties both here and overseas and who spend at least 30 days abroad in a tax year. This relief too has lost its rationale, which harks back to the days of penalty 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. For the same reason, I propose to withdraw the matching relief for the self-employed who spend 30 days abroad, and for resident employees and self-employed 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 have also authorised the Inland Revenue to consult interested parties about a possible relaxation in the rules governing the taxation of expenses reimbursed to employees for travel overseas. I am not making any change to the 100 per cent deduction given for absences abroad of 365 days or more.

112. 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.

113. 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 accordingly proposing an increase of 10 per cent in both the car and car fuel scales with effect from April 1985.

114. 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 way out of line with comparable rates abroad, and with the top rates of other taxes in this country. I propose therefore to reduce the highest rate of capital transfer tax from 75 per cent to 60 per cent and to raise the threshold to £64,000 in line with indexation. [For lifetime gifts I further propose to make the rate one-half of that on death over the whole scale.]

*Misleading*

115. 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 in a later year.



116. 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 numbers affected by the tax by more than one-third.

117. Next share options. The measures introduced in the last Parliament to improve employee involvement through profit sharing and savings related share option schemes have been a notable success. The numbers of all these employee schemes have 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 the gift of shares in the employee's company.

118. 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 will be taken out of income tax, 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 conditions which are granted from 6 April, ~~1981~~.

119. 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.

120. Before turning to North Sea taxation, I should like to remind the House of the Government's concern at the threat which the spread of unitary taxation in certain US states has posed to the US subsidiaries of British firms. With our European partners we are monitoring the situation closely, and await with keen interest the imminent report of a Working Group under my US counterpart. It is very important that a satisfactory solution be speedily implemented.

121. This issue is not wholly irrelevant to the North Sea, for US firms operating there, or elsewhere in this country, are not of course taxed on a unitary basis, taking account of world-wide profits.

DRAFT NORTH SEA PASSAGE FOR BUDGET SPEECH

Al. h. g. m. c.

122. Last year's North Sea tax changes were well received, and there has been encouraging progress in the number of development projects coming forward, as well as in exploration and appraisal. The Government is 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 <sup>my vt has filed</sup> 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.

123. Meanwhile, I am taking two measures to prevent an unjustified loss of tax in 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 concluded that this can no longer be justified. I have also reviewed the case for extending last year's future field concessions to the Southern Basin, but have concluded that additional incentives here are not needed. //

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

125. Ever since VAT was introduced in this country, we have treated imports differently from the way in which they are treated by our main European Community competitors. In a nutshell, 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. This is an advantage not enjoyed by the home-produced equivalent of the import, since businesses buying from UK suppliers have to pay VAT when they pay their suppliers.

126. The UK system does indeed have many advantages, which is why the European Commission has for some years now been seeking to get it adopted throughout the Community, with the full support of both my predecessor and myself. But the plain fact is that in all that time the Commission has made no progress whatever.

127. 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 ~~we~~ agree that the Commission's proposal should be accepted after all, then of course we would gladly revert to the present system. But in the meantime I propose to move to the system used by our major competitors and charge VAT straight away on imports, providing the same facilities for deferring payment 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.



128. 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 of course be ~~borne~~ <sup>borne</sup> by foreign producers and manufacturers. There will naturally be no increased revenue in subsequent years.

129. The second change I propose to make on 1 October concerns the National Insurance Surcharge. This, once again, was a brainchild of the Rt Hon member for Leeds East. Having introduced it in 1977 at the rate of 2 per cent, he then raised it in 1978 to 3½ per cent. During the last Parliament, my predecessor succeeded in reducing it to 1 per cent, and we are pledged to abolish it during the lifetime of this Parliament.

130. 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.

131. Thus my proposals offer British business the abolition of the tax on jobs and the reduction of the rate of taxation on profits. They also sweep away a number of out-dated reliefs, reduce distortions, and assist enterprise.



CH/EX REF. NO. B(84) 566

FROM: MISS M O'MARA

DATE: 8 March 1984

cc Sir P Middleton  
Mr Cassell  
Mr Lankester  
Mr Pirie  
Mr Plett  
Mr Catlin - T/Sol.

PS/ECONOMIC SECRETARY

**TRUSTEE SAVINGS BANKS: LEGISLATION**

The Chancellor has seen Mr Pirie's minute of 7 March and agrees with his advice. He has stressed that the idea of a joint TSB/Building Society Bill must on no account be revealed to anyone until we and Parliamentary Counsel have thoroughly explored the possibility.

*MOM*

MISS M O'MARA





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

FOREIGN AND COMMONWEALTH SECRETARY

VERMOUTH

Many thanks for your minute today. I have thought hard about your suggestion, but I honestly don't think it works. If we mention vermouth without mentioning the Italians people will think we are complaining about the French as well as the Italians. And I honestly don't see how that improves the picture diplomatically.

2. What I will do, in the light of your comments, is put some water in the vermouth paragraph. It can certainly be toned down a bit, but I am sure that it has to refer to the Italians if it's to make sense.

A handwritten signature in black ink, appearing to be 'N.L.' with a flourish.

N.L.

8 March 1984



CH/EX REF. NO. B(84) 569

FROM: MISS M O'MARA

DATE: 9 March 1984

cc PS/Chief Secretary  
PS/Financial Secretary  
PS/Minister of State  
PS/Economic Secretary  
Sir P Middleton  
Mr Bailey  
Mr Cassell  
Mr Monck  
Mr Battishill  
Mr Lovell  
Mr Monger  
Mr R I G Allen  
Mr Lord  
PS/IR  
Mr Graham - Parly. Counsel

MR BEIGHTON - INLAND REVENUE

**SHIPPING: MR RIDLEY'S LETTER OF 7 MARCH**

The Chancellor has seen your minute of 8 March. He does not want to offer the concession on the BES which you have identified.

*Mom*

MISS M O'MARA





FROM: MISS M O'MARA

DATE: 9 March 1984

Mr Corlett - Inland Revenue

cc PS/Chief Secretary  
PS/Financial Secretary  
PS/Economic Secretary  
Mr Monck  
Mr Battishill  
Mr Lovell  
Mr Monger  
Mr R I G Allen  
Mrs Lomax  
Mr Lord  
Mr Portillo  
PS/Inland Revenue

CAPITAL ALLOWANCES: PRESS NOTICE: ENTERPRISE ZONES

This is to confirm that the Chancellor has seen your minute of 8 March and Mr Hudson's minute of today and endorses the Financial Secretary's recommendation.

*MOM*

MISS M O'MARA



CH/EX REF. NO. B(84) 579COPY NO 26 OF 28 COPIES

FROM: MISS M O'MARA

DATE: 9 March 1984

cc PS/Chief Secretary  
 PS/Minister of State  
 PS/Economic Secretary  
 Sir P Middleton  
 Sir T Burns  
 Mr Bailey  
 Mr Littler  
 Mr Byatt  
 Mr Cassell  
 Mr Monck  
 Mr Battishill  
 Mr Lovell  
 Mr Monger  
 Mr Smee  
 Mr Allen  
 Mr Folger  
 Mr Norgrove  
 Mr Ridley  
 Mr Lord  
 Mr Portillo  
 PS/IR  
 Mr Beighton - IR  
 PS/C&E

PS/FINANCIAL SECRETARY

**THE BUDGET AND BUSINESS:****THE TREASURY PRESS NOTICE AND BRIEFING ON SECTORAL IMPACT**

The Chancellor has seen both Mr Monck's and Mr Ridley's minutes of 8 March covering different versions of the Treasury Press Release. His preference is for Mr Monck's version *with the following amendments:*

Paragraph 7 line 1: Amend to "... certain types of capital investment ...."

Paragraph 13 line 3: Delete "some".

Paragraph 14 line 1: Amend to "Stock relief was introduced as a rough-and-ready measure to counter ...."

Paragraph 14 line 5: Amend to "... It will also simplify the system ...."





I have already passed these comments to Mr Monck.

2. Although the Chancellor felt that the Ridley/Allen versions of the Press Release were too long for that purpose, he has commented that they contain some very useful speech material and should be used as such.

*Mon*  
MISS M O'MARA



Ch/Ex Ref No

B.(84)580



FROM: MISS J C SIMPSON

DATE: 9 MARCH 1984

PS/FST

cc PS/CST  
 PS/EST  
 Mr Monger  
 Mr Allen  
 Mrs Lomax  
 Mr Willetts  
 Mr Lord  
 PS/IR  
 Mr Bryce/IR

## BUDGET DAY PRESS RELEASE: CAPITAL GAINS TAX ITEMS

The Chancellor has seen the press release attached to Mr Bryce's minute of 8 March.

2. He is not happy with (ii) on the press release (the piece relating to corporate bonds). As presently drafted, this implies that exemption is being granted to some special category of corporate bonds. As the Chancellor has pointed out, in fact the exemption is a general one for all new corporate bonds issued by quoted (or USM) companies, subject only to some necessary restrictions. He has asked that the press release should be re-done in this sense. You should note that the same objection will apply to paragraphs 3-6 of the background note for editors.

B

MISS J C SIMPSON  
 Private Secretary





Ch/Ex Ref No B(84)581...

FROM: MISS J C SIMPSON  
 DATE: 9 MARCH 1984

PS/FST

cc PS/CST  
 PS/MST  
 PS/EST  
 Sir P Middleton  
 Mr Cassell  
 Mr Monger  
 Mr Battishill  
 Ms Conn  
 Mr R I G Allen  
 Mr Lord  
 Mr Portillo  
 PS/IR  
 Mr Lusk/IR

## TAX TREATMENT OF FURNISHED HOLIDAY LETTINGS

The Chancellor has seen and was grateful for your minute of 8 March giving the Financial Secretary's conclusions.

2. He has commented that the concession at paragraph 2 (c) is not one the Government is committed to make. It is one which it will make only if it judges the pressure to be such that a concession in Committee would be wise. No hint of it should emerge at this stage. For the record, he does think that the odds are that it will be necessary to make the concession, but that will remain to be seen.

3. He is also content that there should be no mention of holiday lettings at all in the Budget Speech.

B

MISS J C SIMPSON  
 Private Secretary





CH/EX REF NO B(84)587

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

9 March 1984

The Rt. Hon. Peter Walker MBE MP  
Secretary of State for Energy

- PS/CST
- PS/FST
- Mr Cassell
- Mr Monck
- Mr Monger
- Mr R I G Allen
- Mr Robson
- Mr Hall (IDT)
- Mr Portillo
- Mr Ridley
- Mr Crawley - IR

**BUDGET PUBLICITY - NORTH SEA**

At our meeting on 27 February on the Budget proposals for the North Sea we agreed that I would let you see the North Sea section of my Speech, and that your people would show mine the text of your press release after Budget Day.

We have been giving further thought at our end to how the Budget should be presented generally and I have concluded that it would be undesirable - and possibly counter-productive for the oil industry itself - to draw attention in my Speech, or accompanying presentational documents such as our Press Releases or the proposed letter to UKOOA - to the North Sea's overall net gains from the Budget, or the further improvement to profitability of future fields. The enclosed paragraphs of my draft Speech reflect this conclusion.

The whole thrust of the Budget is to remove special reliefs for one sector or special interest or another. If we start drawing attention to the gainers, we will only encourage people to ask who the losers are, and to attack the package on distributional grounds. I therefore think it is important not to be drawn on the impact for particular sectors. The industry (and experienced commentators like Wood Mackenzie) will rapidly do their own sums, and I do not see any reason to expect activity or confidence to be damaged if we avoid a presentation which, while perhaps prima facie more helpful in relation to the North Sea taken in isolation, could have unhelpful repercussions on the overall package.

The same considerations apply of course to the idea of a Press Release.\*

A copy of this letter goes to Norman Tebbit.

NIGEL LAWSON

\* I am, however, content for the budgetary effects on the North Sea to be pointed out in off-the-record speeches. This should meet the interests of Alex & John Moore. JL



BUDGET SECRET

DRAFT NORTH SEA PASSAGE FOR BUDGET SPEECH

Last year's North Sea tax changes were well received, and there has been encouraging progress in the number of development projects coming forward, as well as in exploration and appraisal. The Government is 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 Rt 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 in 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 concluded that this can no longer be justified. I have also reviewed the case for extending last year's future field concessions to the Southern Basin, but have concluded that additional incentives here are not needed.





CH/EX REF NO B(84)588

FROM: MISS J C SIMPSON

DATE: 9 March 1984

MR MOWL

- cc PS/Chief Secretary
- PS/Financial Secretary
- PS/Minister of State
- PS/Economic Secretary
- Sir P Middleton
- Sir T Burns
- Mr Littler
- Mr Bailey
- Mr Cassell
- Mr Evans
- Mr Battishill
- Mr Odling-Smee
- Mr Sedgwick
- Mr Lankester
- Mrs Lomax
- Mr Riley
- Mr Shields
- Mr Ridley
- Mr Lord
- Mr Portillo

PROVISIONAL POST-BUDGET FINANCIAL FORECAST

The Chancellor has seen, and was grateful for your minute of 8 March. He has only one comment to make; in the last paragraph, he has noted that in 1982 only one-third of new life business qualified for tax relief anyway. He has asked that this should be included in the defensive briefing package for LAPR.

*B*

MISS J C SIMPSON





CH/EX REF NO B(590)24  
 COPY NO 25 OF 28 COPIES  
 FROM: MISS M O'MARA  
 DATE: 9 March 1984

SIR PETER MIDDLETON

cc PS/Chief Secretary  
 PS/Financial Secretary  
 PS/Minister of State  
 PS/Economic Secretary  
 Sir T Burns  
 Mr Bailey  
 Mr Cassell  
 Mr Monck  
 Mr Battishill  
 Mr Evans  
 Mr Lankester  
 Mr Odling-Smee  
 Mr Scholar  
 Mr Folger  
 Mr M Hall  
 Mrs Lomax  
 Mr Riley  
 Mr S Davis  
 Mr Ridley  
 Mr Lord  
 Mr Portillo

PRESENTATION OF THE MTFS AND THE LTPE

The Chancellor was grateful for your minute of 8 March, covering briefs by Mr Scholar and Mr Riley. He had the following comments:-

MTFS

Key themes (b)(vii): The Chancellor has commented that a little more scepticism is needed about M2.

Pitfalls (a)(i): Penultimate line. Amend to "... policy was significantly tightened but when ...."

Pitfalls (a)(v): The Chancellor would prefer the second and third sentences to be deleted. He has commented that we might just as well have inflation targets if we go as far as this.

Pitfalls (a)(ix): Replace second sentence with "but we expect it within the LTPE horizon."





Pitfalls (a)(x): The Chancellor has commented that 2½ per cent is not a forecast and that this needs to be made clear.

Pitfalls (a)(xi): Amend first sentence to "Assumption of 2½ per cent a year is about the average ...."

Pitfalls (a)(xii), line 3: Replace "within" with "during".

Pitfalls (a)(xiv): Delete second sentence. Amend third sentence to read: "The fiscal adjustments in 1987-88 and 1988-89 could in principle ..."

Pitfalls (b)(ii): Amend to "Encapsulating both broad and narrow money in one target range has been possible in the last two years only because in the particular circumstances of the time, the growth of M1 and the broad aggregates were not expected to be very different. But growth of M0 can normally be expected ..."

Pitfalls (b)(iv), line 9: Delete "quite".

Pitfalls (b)(v), line 9: Delete "eg M2".

Pitfalls (b)(x): No answer is shown here! The Chancellor suggests it should read "The sort of stability to which we have become accustomed in recent years."

Pitfalls (c)(i): Amend to " - the PSBR was higher than intended in 1983-84."

Pitfalls (c)(v): Amend penultimate sentence to read: "The profile is consistent with a continuing decline in inflation." Delete final sentence.

Pitfalls (c)(viii): The Chancellor does not like the reference to GGFD in the final sentence. He suspects that commentators would point out that the PSBR does not take into account the profitability of the private sector, which equally clearly affects the economy.





Pitfalls (c)(ix): The Chancellor has added "Anyone can add back asset sales if they so wish: the right question is not the precise definition of the PSBR; it is whether, given the definition, it is of an appropriate size."

Pitfalls (c)(xii): The Chancellor has commented that surely the IFS calculations of public sector balance sheets are highly conjectural.

LTPE

Defensive (i): The Chancellor has noted that in any event the Government did not consider such figures at all reliable.

Defensive (vi): The Chancellor has suggested that the case for prudence should be noted, as stated in the Green Paper itself.

Defensive (xi): Delete final sentence.

Defensive (xiv), line 1: substitute "by" for "before".

As you will have gathered, the Chancellor agrees that it would be best to make very little use of the 3 per cent inflation assumption at the end of the MTFs. He has also endorsed Mr Scholar's suggestions about the key groups to be approached, the possibility of a helpful article and the production of a Ministerial briefing pack (paragraph 3 of his minute of 7 March).

*mm*

MISS M O'MARA





Ch/Ex Ref No B(84).601

FROM: MISS M O'MARA  
DATE: 9 March 1984

Sir Lawrence Airey  
Customs & Excise

cc PS/Chief Secretary  
PS/Financial Secretary  
Sir P Middleton  
Mr Bailey  
Mr Anson  
Mr Monger

MANPOWER IMPLICATIONS OF THE BUDGET

The Chancellor has seen your minute of 8 March and is entirely content with the line you propose to take.

*mom*

MISS M O'MARA



FROM: T BURNS  
DATE: 9 MARCH 1984

7  
SIR PETER MIDDLETON

**DISTRIBUTIONAL ANALYSIS OF THE BUDGET/IFS**

Thank you for your minute of 8 March. I have spoken to Mr Smith and we agreed that he would not persue the work at the moment. There was a danger of it attracting some undesirable attention and it is not clear what we can learn at this stage. In any case IFS will be doing their own analysis and on past form it is unlikely to be produced in a manner that is favourable to the Treasury. We agreed that he would look at the IFS analysis at a more liesurely pace.

2. I mentioned to him that you had raised the question of our own in-house capability and what we were getting for our support of the IFS research work. He said that he would take this up later. You could raise it in the general context of the research budget when you have received answers to your initial queries. Apparantly there are a number of these exercises around - Revenue Departments, DHSS, CSO - but they are all slightly different. Setting up our own capability might not be a simple matter but I share your instinct that the present system is not satisfactory.



**T BURNS**





Ch/Ex Ref No B(84).601

FROM: MISS M O'MARA  
DATE: 9 March 1984

Sir Lawrence Airey  
Customs & Excise

cc PS/Chief Secretary  
PS/Financial Secretary  
Sir P Middleton  
Mr Bailey  
Mr Anson  
Mr Monger

MANPOWER IMPLICATIONS OF THE BUDGET

The Chancellor has seen your minute of 8 March and is entirely content with the line you propose to take.

*mom*

MISS M O'MARA



CH/EX REF NO B(84)610

FROM: J O KERR

DATE: 10 March 1984

MR KNOX - Customs &amp; Excise

cc PS/Chief Secretary  
 PS/Financial Secretary  
 PS/Minister of State  
 PS/Economic Secretary  
 Sir P Middleton  
 Mr Fraser (C&E)  
 Mr Littler  
 Mr Cassell  
 Mr Monger  
 Mr Battishill  
 Mr Griffiths  
 Mr Norgrove  
 Mr Polge

VERMOUTH

This is to confirm that the Chancellor last night accepted your advice that the developments reported in Rome telegram no 157 constituted sufficient progress to justify dropping the proposed vermouth surcharge from the Budget Speech, Resolutions, FSBR, and briefing. And he and the Foreign Secretary were content with the anodyne replacement paragraph for the Speech, referring to an "undertaking" from the Italians. These decisions are final.

2. The Chancellor will welcome your further advice on the acceptability of the letter from Pandolfi conveyed in Rome telegram no 159 today.

3. If we in due course find that the Italians do not live up to their undertaking, the Chancellor envisages that we might introduce a vermouth surcharge clause at the Committee stage of the Finance Bill. We could then of course refer back to the anodyne paragraph in the Budget Speech.

A handwritten signature in dark ink, appearing to be 'J O Kerr'.

J O KERR





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

10 March 1984

Andrew Turnbull Esq  
10 Downing Street

*Dear Andrew,*

BUDGET SPEECH

- .. I enclose the latest, and very nearly final, text of the Budget Speech. You will see that the Chancellor has taken considerable account of the points which you mentioned to me last night.

*Yours ever,*  
*J O K*  
J O KERR



BUDGET SECRET



B(84)612

cc. Sir P. Middleton  
Mr Cause II

SPARE.

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

10 March 1984

John Bartlett Esq  
Private Secretary to the  
Governor  
Bank of England

*Dear John,*

BUDGET SPEECH

.. I attach, for the Governor's information, the (very nearly final) text of the Budget Speech. I know that you and he will ensure that it is very carefully handled.

*Yours ever,*  
*J O Kerr*  
J O KERR





Ch/Ex Ref No B(84)623

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

9 March 1984

Christopher Tugendhat Esq  
Vice-President of the Commission of the  
European Communities  
Rue de la Loi 200  
1049 Brussels

A handwritten signature in cursive script, appearing to read 'Chris Christopher'.

I have not replied sooner to your two letters of 22 February because I wanted to give you a considered answer in the light of my Budget decisions. Some of the indirect tax changes which I shall announce on Tuesday have significant Community implications, and I have tried in this letter, which will be delivered to you as soon as the Budget Statement has been made, to set out the relevant background.

First, VAT. I have decided to suspend as from 1 October the arrangement for postponed accounting for VAT on imports. You are right, of course, to point to the attraction of the cash-flow gain to the Exchequer; this has made a very important contribution to a major reforming Budget. I am sure you will understand how vital it is to get things on the right track now - early in the life of this Parliament - if we are to realise our aims of significantly reducing the tax burden before the end of the decade.

But the cash-flow point is not the principal reason for the change. The fact is that our present arrangements have an in-built bias in favour of imports. This is because there is no financing cost to importers in respect of import VAT, whereas purchasers of similar goods within the UK must, unless they can get very generous credit terms from their suppliers, finance the VAT for at least some of the period (which averages about 11 weeks) before they can claim the VAT back from Customs. Pressure has been building up to redress this situation. I felt I could no longer ignore it so long as there was no off-setting advantage elsewhere. So the average period of delay for most importers will come down to 4 weeks.





This brings me to the proposed 14th Directive. You really don't need to remind me of the strong UK support for this proposal, which I shall reaffirm in the House. Indeed I shall give an undertaking in my Budget Speech to reintroduce postponed accounting as and when the Community agrees to adopt it as the basis for harmonisation. This is an unconditional commitment. But I hope you will understand that the UK cannot indefinitely 'go-it-alone' while our major EC competitors retain VAT systems less biased in favour of imports than ours.

On other VAT changes, the extensions to the base are a crucial part of my policy of switching from taxes on income to taxes on spending. Any extension of VAT into areas that were previously relieved is bound to be highly sensitive politically. But the items I have chosen to tax were in fields where the case for continuing relief was least strong. You will undoubtedly be disappointed that I could not act on the zero-rated items which are in dispute between us. I am afraid that the Commission's failure so far to convince me of its case, combined with the political delicacy of the issues involved, means that we must continue to differ.

I have raised the VAT registration threshold in line with inflation since 1973, as I am persuaded that to do so is both in accordance with a proper interpretation of the Sixth Directive (and the ancillary statements recorded with its adoption) and right in principle in order to keep as many small traders as possible out of the VAT net. In the present economic circumstances I see no sense in stifling with bureaucracy the entrepreneurial spirit of the small business sector.

Turning now to the duties on alcoholic drinks, you will see that I have reduced the duty on wine and raised that on beer in order to comply fully with the European Court's judgement. The new ratio between the duties is just under 3 to 1 and accords with the requirements of article 95 of the Treaty; and I have neither restructured the wine duty nor attempted to phase the change over two or more Budgets. I am sure you will agree that my action is compatible with your proposals to revive discussion of harmonisation of excise duties on alcoholic beverages.

In changing the duties on drinks I have gone further. The rates of duty on made wine are now fully aligned with those on wine of fresh grapes, and cider containing between 8.5 and 8.7 per cent alcohol has been brought into the made wine category. There is now therefore no difference in the fiscal treatment of wine and made wine, and I trust the Commission will feel able to drop proceedings on this matter.

My officials are today going over the details of these changes with your people in DG XV. But I thought it right to tell you personally what lay behind my decisions.



CH/EX REF NO B(84) 614

FROM: J O KERR

DATE: 10 March 1984

SIR PETER MIDDLETON

cc Chief Secretary  
Financial Secretary  
Minister of State  
Economic Secretary  
Sir T Burns  
Mr Fraser (C&E)  
Mr Battishill  
Mr Monger  
Mr Ridley  
Mr Lord  
Mr Portillo  
Mr Norgrove  
Mr Knox: C&E  
Mr Folger

BUDGET SPEECH

I attach the near-final text of the Speech. It reflects further work by the Chancellor on 9/10 March.

2. In preparing this version, the Chancellor considered all amendments offered to the previous version. Any further suggested amendments should reach me by 1pm on 12 March: this is I fear a real deadline. But there is of course no need for copy addressees to repeat suggestions previously made, unless an inaccuracy has [inadvertently] not been corrected.

A handwritten signature in dark ink, appearing to be 'J O Kerr'.

J O KERR



## INTRODUCTION

THIS BUDGET WILL SET THE GOVERNMENT'S COURSE FOR THIS PARLIAMENT. THERE WILL BE NO LETTING UP IN OUR DETERMINATION TO DEFEAT INFLATION. THIS BUDGET WILL CONTINUE THE POLICIES THAT WE HAVE FOLLOWED CONSISTENTLY SINCE 1979. THOSE POLICIES PROVIDE THE ONLY WAY TO ACHIEVE OUR ULTIMATE OBJECTIVE OF STABLE PRICES. TO LET THEM GO 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 'SIXTIES. GROWTH IN THE ECONOMY IS STRONG. EMPLOYMENT IS GROWING.

2. THOSE ACHIEVEMENTS ARE A TRIBUTE TO THE COURAGE AND FORESIGHT OF THE FIVE BUDGETS PRESENTED BY MY DISTINGUISHED PREDECESSOR, WHOSE DUTIES SADLY KEEP HIM IN BRUSSELS TODAY.

/My BUDGET



BUDGET SECRET

3. I SHALL DO NOTHING TODAY TO COMPROMISE THOSE SUCCESSES. BUT THERE IS MUCH THAT I CAN DO TO BUILD UPON THEM.

4. MY BUDGET TODAY HAS TWO THEMES.

5. FIRST, THE FURTHER REDUCTION 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.

6. 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.



BUDGET SECRET

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.

7. 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

8. I START WITH THE ECONOMIC BACKGROUND.
9. SINCE 1980, INFLATION HAS FALLEN STEADILY FROM A PEAK OF OVER 20 PER CENT. LAST YEAR IT WAS DOWN TO ABOUT  $4\frac{1}{2}$  PER CENT, THE LOWEST FIGURE SINCE THE SIXTIES. AND WITH LOWER INFLATION HAVE COME LOWER INTEREST RATES.
10. 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.

/ACROSS THE



BUDGET SECRET

11. 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.

12. 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 DURING 1983 MANUFACTURING PRODUCTIVITY GREW BY 6 PER CENT WITH NO SIGN OF SLOWING DOWN. 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



BUDGET SECRET

13. 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 ALMOST 200,000 IN THE FIRST NINE MONTHS OF LAST YEAR.

14. 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 US, 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.

15. 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



BUDGET SECRET

CENT COMPARED WITH 1982. FIXED INVESTMENT ROSE RATHER FASTER THAN CONSUMPTION, WITH INVESTMENT IN HOUSING AND SERVICES PARTICULARLY STRONG.

16. 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.

17. OUR CRITICS HAVE BEEN CONFOUNDED BY THIS COMBINATION OF RECOVERY AND LOW INFLATION. EVEN THE PESSIMISTS HAVE BEEN FORCED TO ACKNOWLEDGE THE DURABILITY OF THE RECOVERY. IT IS SET TO CONTINUE

/THROUGHOUT



## BUDGET SECRET

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.

18. LOOKING ABROAD, TOO, ECONOMIC PROSPECTS ARE MORE FAVOURABLE THAN 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.

19. 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



## BUDGET SECRET

AND THE NEED TO FINANCE THE US 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.

20. A SECOND POTENTIAL RISK IS DISRUPTION IN THE OIL MARKET. THE UNITED KINGDOM, AND INDEED THE WORLD ECONOMY, INEVITABLY REMAIN VULNERABLE TO ANY MAJOR DISTURBANCES IN THIS MARKET.

21. 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 MTFS

22. 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 ABANDONED FINANCIAL DISCIPLINE WHENEVER THE GOING GOT ROUGH, AND STAGGERED FROM ONE SHORT-TERM POLICY EXPEDIENT TO ANOTHER. THE TEMPTATION TO ACCOMMODATE INFLATIONARY PRESSURES PROVED IRRESISTIBLE, AND THE NATION'S LONGER-TERM ECONOMIC PERFORMANCE WAS PROGRESSIVELY UNDERMINED.

/THE MTFS WAS



## BUDGET SECRET

23. THE MTFS 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.

24. PEOPLE NOW KNOW THAT THE GOVERNMENT INTENDS TO STICK TO ITS 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.

25. ORIGINALLY THE MTFS COVERED FOUR YEARS. IN THIS FIRST BUDGET OF A NEW PARLIAMENT IT IS

/APPROPRIATE TO



## BUDGET SECRET

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 LAST TWO YEARS OF THE NEW MTFS, WHICH LIE BEYOND THE PERIOD COVERED IN LAST YEARS PUBLIC EXPENDITURE SURVEY AND LAST MONTH'S WHITE PAPER, THE GOVERNMENT HAS 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



BUDGET SECRET

26. THE PRECISE FIGURES SET OUT IN THE MTFS ARE NOT OF COURSE A RIGID FRAMEWORK, LACKING ALL FLEXIBILITY. AS IN THE PAST, THERE MAY WELL 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**

27. MONETARY POLICY WILL CONTINUE TO PLAY A CENTRAL ROLE. FURTHER REDUCTIONS IN MONETARY GROWTH ARE NEEDED TO ACHIEVE STILL LOWER INFLATION.

28. OVER THE TWELVE MONTHS TO MID-FEBRUARY THE GROWTH OF £M3 HAS BEEN WELL WITHIN THE 7-11 PER CENT TARGET RANGE, WITH M1 AND PSL2 AT OR A LITTLE ABOVE THE TOP OF 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.

/OTHER EVIDENCE



BUDGET SECRET

29. OTHER EVIDENCE CONFIRMS THAT MONETARY CONDITIONS ARE SATISFACTORY. THE EFFECTIVE EXCHANGE RATE HAS REMAINED FAIRLY STABLE, DESPITE THE INTERNATIONAL UNCERTAINTIES WHICH I HAVE DESCRIBED.

30. 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 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.

31. ONE IMPORTANT DEVELOPMENT HAS BEEN THE ATTEMPT TO GIVE A MORE EXPLICIT ROLE TO THE NARROW MEASURES OF MONEY.  $M3$  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,



## BUDGET SECRET

OF SAVINGS, INVESTED FOR THE INTEREST IT CAN EARN. IN DEFINING POLICY IT IS HELPFUL ALSO TO MAKE SPECIFIC REFERENCE TO MEASURES OF MONEY WHICH RELATE MORE NARROWLY TO BALANCES HELD FOR CURRENT SPENDING.

32. 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.

33. OTHER MEASURES OF NARROW MONEY HAVE NOT BEEN DISTORTED TO THE SAME EXTENT. IN PARTICULAR, M0, 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



BUDGET SECRET

A USEFUL GUIDE BUT, BEING NEW, STILL NEEDS TO BE INTERPRETED WITH PARTICULAR CARE.

34. 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.

35. THE TARGET RANGE FOR BROAD MONEY WILL CONTINUE TO APPLY TO £M3, AND FOR THE COMING YEAR WILL BE SET AT 6-10 PER CENT, AS INDICATED IN LAST YEAR'S MTFS. THE TARGET RANGE FOR NARROW MONEY WILL APPLY TO M0 AND FOR NEXT YEAR WILL BE SET AT 4-8 PER CENT. TO AVOID ANY POSSIBLE MISUNDERSTANDING, LET ME STRESS THAT THE USE OF M0 AS A TARGET AGGREGATE WILL NOT INVOLVE ANY CHANGE IN METHODS OF MONETARY CONTROL.

/THE TWO TARGET



## BUDGET SECRET

36. 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.

37. 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 THE NATIONAL SAVINGS WILL REMAIN IMPORTANT. THIS YEAR'S NATIONAL SAVING'S TARGET OF £3 BILLION IS LIKELY TO BE ACHIEVED: THE TARGET FOR THE COMING YEAR WILL AGAIN BE £3 BILLION.

/PRECISE MONETARY



BUDGET SECRET

38. 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 MTF'S, 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**

39. 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 DOES THE MEDIUM TERM FINANCIAL STRATEGY.

40. 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 3½ PER CENT OF GDP.

41. SINCE THEN 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



## BUDGET SECRET

AROUND £10 BILLION, EQUIVALENT TO  $3\frac{1}{4}$  PER CENT OF GDP. THIS IS SIGNIFICANTLY ABOVE WHAT WAS INTENDED AT THE TIME OF LAST YEAR'S BUDGET, AND WOULD OF COURSE HAVE BEEN HIGHER STILL HAD IT NOT BEEN FOR THE JULY MEASURES.

42. 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, UK LONGER-TERM RATES ARE NOW LONGER THAN AMERICAN RATES. AS LONG AS AMERICAN RATES REMAIN NEAR THEIR CURRENT LEVEL, IT IS HIGHLY DESIRABLE THAT THIS ADVANTAGE BE MAINTAINED.

43. THE HIGHER LEVEL OF ASSET SALES WE ARE PLANNING AS THE PRIVATISATION PROGRAMME GATHERS PACE IS A

/FURTHER REASON



BUDGET SECRET

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.

44. LAST YEAR'S MTF'S SHOWED AN ILLUSTRATIVE PSBR FOR 1984-85 OF  $2\frac{1}{2}$  PER CENT OF GDP, EQUIVALENT TO AROUND £8 MILLION. 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  $2\frac{1}{4}$  PER CENT OF GDP, OR £7½ BILLION.

45. 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

/£7½ BILLION



BUDGET SECRET

£7¼ BILLION WILL REQUIRE NO OVERALL NET INCREASE TAXATION.

46. 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 £1¼ 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.



**PUBLIC EXPENDITURE**

47. 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.

48. 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 WAGE SCALE.

49. 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



BUDGET SECRET

50. 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.

51. THE GOVERNMENT IS THEREFORE PUBLISHING TODAY, IN ADDITION TO THE CUSTOMARY BUDGET DOCUMENTS, A GREEN PAPER ON THE PROSPECTS FOR PUBLIC SPENDING AND TAXATION OVER THE NEXT TEN 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.

52. 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



BUDGET SECRET

TO THE LEVELS OF THE EARLY 1970s ONLY IF PUBLIC SPENDING IS KEPT BROADLY STABLE IN REAL TERMS OVER THE NEXT TEN YEARS.

53. THE GOVERNMENT BELIEVES THAT THE ISSUES DISCUSSED IN THE GREEN PAPER MERIT THE ATTENTION OF THE HOUSE AND THE COUNTRY.

54. IN CONTRAST TO PREVIOUS YEARS, I HAVE NO PACKAGE OF PUBLIC EXPENDITURE MEASURES TO ANNOUNCE IN THIS BUDGET. THE WHITE PAPER PLANS STAND.

55. 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 THEM AMONG OTHER THINGS TO SECURE THE FUTURE OF CALKE ABBEY. MY RT HON FRIEND THE SECRETARY OF STATE FOR THE ENVIRONMENT WILL BE ANNOUNCING THE DETAILS SHORTLY.

/THE HOUSE WILL



BUDGET SECRET

56. 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 UPDATING, PRICE PROTECTION IS MEASURED BY REFERENCE TO THE RETAIL PRICE INDEX FOR MAY. MY RT 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.

57. BEFORE LEAVING GOVERNMENT SPENDING, I SHOULD ADD A WORD ON PUBLIC SECTOR MANPOWER. AT THE BEGINNING OF THE LAST PARLIAMENT, THE GOVERNMENT SET ITSELF 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



BUDGET SECRET

SMALLER CIVIL SERVICE WILL CONTINUE TO IMPROVE ITS EFFICIENCY. THE TAX CHANGES 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**

58. I MENTIONED 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 SUBSEQUENT BUDGETS.

59. 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.

60. 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



## BUDGET SECRET

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.

61. 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.

62. 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 OF A MAJOR NATURE, 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



BUDGET SECRET

63. 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

64. 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-OWING DEMOCRACY, IN WHICH MORE DECISIONS ARE MADE BY INDIVIDUALS RATHER THAN BY INTERMEDIARY INSTITUTIONS.

65. 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 MACMILLAN GOVERNMENT IN 1963, AND ONCE AGAIN DOUBLED TO 2 PER CENT BY LABOUR IN THE FIRST BUDGET PRESENTED BY THE RT HON MEMBER FOR LEEDS EAST IN 1974. AT ITS PRESENT LEVEL IT IS AN IMPEDIMENT TO MOBILITY AND

/INCOMPATIBLE



BUDGET SECRET

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.

66. I THEREFORE PROPOSE TO HALVE THE RATE OF STAMP DUTY TO 1 PER CENT. WITH THE EXCEPTION OF THOSE DOCUMENTS WHICH HAVE TO BE STAMPED BEFORE 20 MARCH, THE CHANGE WILL TAKE EFFECT FROM TODAY.

67. 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.

68. REDUCING THE RATE OF DUTY ON SHARE TRANSFERS WILL REMOVE AN IMPORTANCE DISINCENTIVE TO INVESTMENT IN EQUITIES AND INCREASE THE

/INTERNATIONAL



## BUDGET SECRET

INTERNATIONAL COMPETITIVENESS OF OUR STOCK MARKET. IT SHOULD ALSO HELP BRITISH COMPANIES TO RAISE EQUITY FINANCE.

69. IN ADDITION, I HAVE THREE 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 EURO BONDS AND 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. SINCE 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



BUDGET SECRET

70. 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.

71. 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. 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 OR INCREASED AFTER TODAY. EXISTING POLICIES WILL NOT BE AFFECTED AT ALL. THE CHANGE IS ESTIMATED TO YIELD ABOUT £90 MILLION IN 1984-85.

72. I AM ALSO PROPOSING TO WITHDRAW THE SPECIAL - BUT UNFORTUNATELY WIDELY ABUSED - PRIVILEGES FOR

/WHAT ARE KNOWN



BUDGET SECRET

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.

73. 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 BUSINESSMAN 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 BE LIABLE TO TAX AT ONLY THE BASIC RATE.

/I HAVE THEREFORE



BUDGET SECRET

74. I HAVE THEREFORE DECIDED THAT THE INVESTMENT INCOME SURCHARGE SHOULD BE ABOLISHED. THE COST IN 1984-85 WILL BE SOME £25 MILLION, BUILDING UP TO £360 MILLION IN A FULL YEAR.

75. 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



## BUDGET SECRET

76. BUT THE MAJOR SOURCE OF UNEQUAL TREATMENT, AGAINST WHICH THE BANKS IN PARTICULAR HAVE FREQUENTLY 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.

77. 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 HAVE TAX DEDUCTED AT THE COMPOSITE RATE. IT HAS NOT HOWEVER STOPPED MANY OF THEM USING BUILDING SOCIETIES BECAUSE OF THE COMPETITIVE RATES 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



BUDGET SECRET

WHILE THE REVENUE ARE SPARED THE NEED TO RECRUIT UP TO 2000 EXTRA STAFF TO COLLECT THE TAX DUE ON INTEREST PAID WITHOUT DEDUCTION.

78. 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.

79. NON-TAXPAYERS WILL 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



## BUDGET SECRET

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.

80. THE TRUE PURPOSE OF THE MOVE IS SIMPLE: FAIRER COMPETITION AND SIMPLICITY ITSELF. UNLESS THEY ARE HIGHER RATE TAXPAYERS, 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. THERE WILL BE NO DIRECT GAIN TO THE EXCHEQUER. HOWEVER, THE INLAND REVENUE WILL BE ABLE TO MAKE STAFF SAVINGS OF UP TO AN EXTRA 1000 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,



## BUDGET SECRET

81. ACCORDINGLY, I PROPOSE TO EXTEND THE COMPOSITE RATE ARRANGEMENTS TO INTEREST RECEIVED BY UK 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.

82. 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. AND THEY WILL REINFORCE THE GOVERNMENT'S POLICY OF ENCOURAGING COMPETITION IN THE FINANCIAL SECTOR, AS IN THE ECONOMY AS A WHOLE.



## BUSINESS TAXATION

83. I NOW TURN TO BUSINESS TAXATION. HERE, GOVERNMENT HAS 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.

84. THE MEASURES 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 THE STRUCTURE OF COMPANY TAXATION.

/RESPONSES TO THE



BUDGET SECRET

85. 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.

86. 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 INVESTMENT DECISIONS AND 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



BUDGET SECRET

WHICH ENCOURAGES LOW-YIELDING OR EVEN LOSS-MAKING INVESTMENT AT THE EXPENSE OF JOBS.

87. 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.

88. 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 (THOUGH NOT COMMERCIAL) BUILDINGS. BUT THERE IS LITTLE EVIDENCE THAT THESE INCENTIVES HAVE STRENGTHENED THE ECONOMY OR IMPROVED THE QUALITY OF INVESTMENT. 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



BUDGET SECRET

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.

89. 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.

90. 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.



BUDGET SECRET

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.

91. 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. I SHOULD ADD THAT, 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 ECONOMIC DEPRECIATION.

/THE CHANGES



BUDGET SECRET

92. THE CHANGES IN THE RATES OF ALLOWANCES WILL NOT APPLY TO PAYMENTS UNDER BINDING CONTRACTS ENTERED INTO ON OR BEFORE TODAY, PROVIDED THAT THE EXPENDITURE IS INCURRED WITHIN THE NEXT THREE YEARS.

93. 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 ANNOUNCED BY MY RT. HON. FRIEND THE SECRETARY OF STATE FOR TRADE AND INDUSTRY IN HIS WHITE PAPER LAST DECEMBER.

/OVER THE SAME



BUDGET SECRET

94. OVER THE SAME PERIOD TO 31 MARCH 1986 MOST OTHER CAPITAL ALLOWANCES WILL BE BROUGHT INTO LINE WITH THE MAIN CHANGES I HAVE ANNOUNCED. THE INLAND REVENUE WILL BE ISSUING A PRESS NOTICE TONIGHT GIVING FULL DETAILS OF THESE PROPOSALS.

95. 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 TO ABOLISH STOCK RELIEF FROM THIS MONTH.

96. THE CHANGES I HAVE JUST ANNOUNCED, IN CAPITAL ALLOWANCES AND STOCK RELIEF, ENABLE ME TO EMBARK ON A MAJOR PROGRAMME OF PROGRESSIVE REDUCTIONS IN THE MAIN RATE OF CORPORATION TAX. FOR PROFITS EARNED IN THE YEAR JUST ENDING, ON WHICH TAX IS GENERALLY

/PAYABLE IN



BUDGET SECRET

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 LESS THAN 17 PERCENTAGE POINTS BELOW THE CURRENT RATE.

97. 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 FOR THE GENERALITY OF PLANT AND MACHINERY WILL BE COMPARABLE WITH THOSE IN MOST OTHER COUNTRIES, WHILE THE RATE OF TAX WILL BE SIGNIFICANTLY LOWER.

98. THE SUBSTANTIAL REDUCTION IN THE RATE OF CORPORATION TAX WILL BRING A FURTHER BENEFIT. OUR

/IMPUTATION SYSTEM



BUDGET SECRET

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, 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.

99. 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



BUDGET SECRET

100. THE CORPORATION TAX MEASURES I HAVE JUST ANNOUNCED WILL COST £280 MILLION IN 1984-85. IN 1985-86 THE COST WILL BE £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 THEY PAY.

101. 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.

102. 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



BUDGET SECRET

- 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.

103. IT IS DOUBTFUL WHETHER IT WAS EVER REALLY SENSIBLE TO SUBSIDISE CAPITAL INVESTMENT IRRESPECTIVE OF THE TRUE RATE OF RETURN. CERTAINLY, WITH OVER THREE MILLION UNEMPLOYED IT CANNOT MAKE SENSE TO DO SO.

104. 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



BUDGET SECRET

105. I NOW TURN TO SOME MORE DETAILED MEASURES AFFECTING BUSINESS.

106. 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.

107. THE SCHEME WAS DESIGNED TO OFFER GENEROUS INCENTIVES FOR INVESTMENT BY 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 TODAY FARMING SHOULD CEASE TO BE TREATED AS A QUALIFYING TRADE UNDER THE SCHEME.

/NEXT, IN KEEPING



BUDGET SECRET

108. NEXT, IN KEEPING WITH WHAT I HAVE SAID ABOUT REMOVING 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.

109. THE FIRST DISTORTION IS THE 50 PER CENT TAX RELIEF (FALLING AFTER 9 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 ABUSE. IT IS, FOR EXAMPLE, POSSIBLE FOR THE SON OF AN IMMIGRANT, WORKING HERE FOR A FOREIGN COMPANY, TO ENJOY THIS RELIEF EVEN IF HE HAS LIVED IN THIS

/COUNTRY ALL HIS



## BUDGET SECRET

COUNTRY ALL HIS LIFE. 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.

110. 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 UK 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 REDUCTION



BUDGET SECRET

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.

111. 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.

112. 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



BUDGET SECRET

113. 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.

114. 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



BUDGET SECRET

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 IN A LATER YEAR.

115. 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.

116. 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 EMPLOYEE SCHEMES OPEN TO ALL EMPLOYEES HAS INCREASED FROM ABOUT 30 IN 1979 TO

/OVER 670 NOW,



BUDGET SECRET

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.

117. 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 WILL BE TAKEN OUT OF INCOME TAX, 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 CONDITIONS WHICH ARE GRANTED FROM 6 APRIL.

/I AM SURE



BUDGET SECRET

118. 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.

119. AS THE HOUSE KNOWS, THE GOVERNMENT IS DEEPLY CONCERNED AT THE THREAT WHICH THE SPREAD OF UNITARY TAXATION IN CERTAIN US STATES HAS POSED TO THE US SUBSIDIARIES OF BRITISH FIRMS. WITH OUR EUROPEAN PARTNERS WE ARE MONITORING THE SITUATION CLOSELY, AND AWAIT WITH KEEN INTEREST THE IMMINENT REPORT OF US TREASURY SECRETARY REGAN'S WORKING GROUP. IT IS ESSENTIAL THAT A SATISFACTORY SOLUTION IS FOUND AND SPEEDILY IMPLEMENTED.

120. US FIRMS OPERATING IN THIS COUNTRY ARE NOT OF COURSE TAXED ON A UNITARY BASIS.

/I NOW TURN



BUDGET SECRET

121. 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. THE GOVERNMENT IS 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 RT 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.

122. MEANWHILE, I AM TAKING TWO MEASURES TO PREVENT AN UNJUSTIFIED LOSS OF TAX IN THE NORTH SEA. FIRST, IN ADDITION TO THE PRT MEASURES ON FARMOUTS WHICH I ANNOUNCED LAST SEPTEMBER, I AM LIMITING THE

/POTENTIAL



BUDGET SECRET

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 ADDITIONAL INCENTIVES HERE ARE NOT NEEDED.

123. I HAVE JUST TWO FURTHER CHANGES AFFECTING BUSINESS TO PROPOSE, BOTH OF WHICH WILL COME INTO FORCE ON 1 OCTOBER.

124. 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,



BUDGET SECRET

RETURN, ON AVERAGE SOME 11 WEEKS LATER. DURING THIS TIME THE IMPORTER ENJOYS FREE CREDIT AT THE TAXPAYER'S EXPENSE. BUT BUSINESSES BUYING FROM UK SUPPLIERS HAVE TO PAY VAT STRAIGHT AWAY.

125. 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.

126. I MUST TELL THE HOUSE HAVE 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



## BUDGET SECRET

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.

127. 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.

128. 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 RT. HON. 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



BUDGET SECRET

129. 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.

130. THE HOUSE WILL I AM SURE AGREE THAT A BUDGET WHICH ABOLISHES THE NATIONAL INSURANCE SURCHARGE, AND 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.

/HAVING



**INDIRECT TAXES**

131. HAVING ANNOUNCED MAJOR REFORMS OF BOTH THE TAXATION OF SAVINGS AND INVESTMENT AND THE TAXATION OF BUSINESS, I TURN NOW TO THE THIRD AND FINAL AREA IN WHICH I PROPOSE TO MAKE PROGRESS ON TAX REFORM. THIS IS THE TAXATION OF PERSONAL INCOME AND SPENDING.

132. 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



BUDGET SECRET

133. 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. THESE CHANGES WILL TAKE EFFECT FROM MIDNIGHT ON THURSDAY. I DO NOT PROPOSE ANY INCREASE IN THE DUTY ON PIPE TOBACCO.

134. 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 AS IT NOW IS, THE NECESSARY INCREASES ARE ON THE WHOLE MERCIFULLY MODEST.

/I PROPOSE TO



BUDGET SECRET

135. I PROPOSE TO INCREASE THE DUTIES ON PETROL AND DERY 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 SIX O'CLOCK THIS EVENING. I DO NOT PROPOSE TO INCREASE THE DUTY ON HEAVY FUEL OIL, WHICH IS OF PARTICULAR IMPORTANCE TO INDUSTRIAL COSTS.

136. 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, AND IT IS WITH THEM IN MIND THAT I PROPOSE TO ABOLISH THE DUTY ON KEROSENE FROM SIX O'CLOCK TONIGHT. I AM SURE THAT THIS WILL BE WELCOMED ON ALL SIDES OF THE HOUSE.

/THE VARIOUS RATES



BUDGET SECRET

137. 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 RT 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.

138. 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



BUDGET SECRET

139. I NOW COME TO THE MOST DIFFICULT DECISION I HAVE 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.

140. IN OUR CASE, THE COMMISSION CONTENDED THAT WE WERE PROTECTING BEER BY UNDER-TAXING IT IN RELATION TO WINE. WE FOUGHT THE CASE, BUT LOST; AND I AM NOW IMPLEMENTING THE JUDGEMENT 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 JUDGEMENT AND MAINTAIN REVENUE: 2P 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



BUDGET SECRET

141. WE HAVE THUS COMPLIED WITH THE COURT'S JUDGEMENT. 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 AN EARLIER COURT RULING ON DISCRIMINATION AGAINST SCOTCH WHISKY AND OTHER IMPORTED SPIRITS.

142. 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.

143. THESE CHANGES IN EXCISE DUTIES WILL, ALL TOLD, BRING IN SOME £840 MILLION IN 1984-85, SOME £200M MORE THAN IS REQUIRED TO KEEP PACE WITH INFLATION.

/THE ADDITION



BUDGET SECRET

THE ADDITION IS OF COURSE DUE TO THE INCREASE IN TOBACCO DUTY.

144. THE REMAINDER OF THE EXTRA REVENUE I NEED TO MAKE A SUBSTANTIAL SWITCH THIS YEAR FROM TAXES ON EARNINGS TO TAXES ON SPENDING WILL 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.

145. 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 GREATLY FROM THE REDUCTION IN THE

/RATE OF STAMP



## BUDGET SECRET

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 SOME 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.

146. 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 RT 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



BUDGET SECRET

147. 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.

148 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 ONE 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  $4\frac{1}{2}$  PER CENT BY THE END OF THE YEAR.

149. 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.



**INCOME TAX**

151. 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.

152. 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



## BUDGET SECRET

153. 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.

154. I HAVE DECIDED THAT, THIS YEAR, THE RIGHT COURSE IS TO USE EVERY PENNY I HAVE IN HAND, WITHIN 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



## BUDGET SECRET

QUICK OR CHEAP SOLUTION TO THESE PROBLEMS. BUT THAT IS ALL THE MORE REASON TO MAKE A FURTHER MOVE TOWARDS SOLVING THEM NOW.

155. I PROPOSE TO INCREASE THE OTHER THRESHOLDS IN LINE WITH THE STATUTORY INDEXATION REQUIREMENT, AND 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 OF £38,100 OR MORE. THE SINGLE AGE ALLOWANCE WILL RISE FROM £2,360 TO £2,490 AND THE MARRIED AGE ALLOWANCE FROM £3,755 TO £3,955.

156. 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 PERSON'S THRESHOLD WILL BE INCREASED BY £220,

/FROM £1,785



BUDGET SECRET

FROM £1,785 TO £2,005; AND THE MARRIED THRESHOLD BY £360, FROM £2,795 TO £3,155.

157. THIS IS AN INCREASE OF AROUND 12½ PER CENT, OR SOME 7 PER CENT IN REAL TERMS. IT BRINGS THE MARRIED MAN'S TAX THRESHOLD 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 FEWER THAN IF THE ALLOWANCES HAD MERELY BEEN INDEXED.

158. 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



BUDGET SECRET

WHICH ROUGHLY HALF REPRESENTS THE COST OF INDEXATION.

159. THIS IS AS FAR AS I CAN GO ON INCOME TAX THIS YEAR, WITHIN A BROADLY REVENUE-NEUTRAL BUDGET FOR 1984-85. BUT AS I HAVE ALREADY SAID, 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 £1½ BILLION, WITH BUSINESS TAKING THE LION'S SHARE.





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

12 March 1984

Roger Bone Esq  
Private Secretary to the  
Secretary of State  
Foreign and Commonwealth Office

*Dear Roger,*

The Chancellor promised to show the Foreign Secretary the text of his letter to Christopher Tugendhat about Budget changes. I now attach a copy of the text.  
..

No action by the FCO is required at this stage: hence the classification of this letter. The letter to Tugendhat is being taken to Brussels by Knox of Customs and Excise, who will contact UKREP tomorrow and ask them to deliver it.

*Yours ever,  
John Kerr*

J O KERR  
Principal Private Secretary



CH/EX REF NO B(84)125

FROM: J O KERR

DATE: 12 March 1984

MR KNOX: Customs &amp; Excise

cc Chief Secretary  
Minister of State  
Economic Secretary  
Sir P Middleton  
Mr Fraser (C&E)  
Mr Littler (or)  
Mr Cassell  
Mr Unwin  
Mr Monger  
Mr Fitchew  
Mr Battishill  
Mr Jefferson Smith (C&E)  
Mr Griffiths

## INDIRECT TAX CHANGES: HANDLING OF THE COMMISSION

.. I attach the final version of the Chancellor's letter to Commissioner Tugendhat. We agreed that you would deliver the top copy, also attached, to Sir Michael Butler tomorrow, with a view to his delivering it to Tugendhat.

2. We have informed UKREP of the existence of the letter, and that you will be bringing it. And, as promised, a copy of the letter has gone to the Foreign Secretary, for information.

A handwritten signature in dark ink, appearing to be 'J O Kerr'.

J O KERR





Ch/Ex Ref No B(84)623

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

9 March 1984

Christopher Tugendhat Esq  
Vice-President of the Commission of the  
European Communities  
Rue de la Loi 200  
1049 Brussels

A handwritten signature in cursive script, appearing to read 'Chris Christopher'.

I have not replied sooner to your two letters of 22 February because I wanted to give you a considered answer in the light of my Budget decisions. Some of the indirect tax changes which I shall announce on Tuesday have significant Community implications, and I have tried in this letter, which will be delivered to you as soon as the Budget Statement has been made, to set out the relevant background.

First, VAT. I have decided to suspend as from 1 October the arrangement for postponed accounting for VAT on imports. You are right, of course, to point to the attraction of the cash-flow gain to the Exchequer; this has made a very important contribution to a major reforming Budget. I am sure you will understand how vital it is to get things on the right track now - early in the life of this Parliament - if we are to realise our aims of significantly reducing the tax burden before the end of the decade.

But the cash-flow point is not the principal reason for the change. The fact is that our present arrangements have an in-built bias in favour of imports. This is because there is no financing cost to importers in respect of import VAT, whereas purchasers of similar goods within the UK must, unless they can get very generous credit terms from their suppliers, finance the VAT for at least some of the period (which averages about 11 weeks) before they can claim the VAT back from Customs. Pressure has been building up to redress this situation. I felt I could no longer ignore it so long as there was no off-setting advantage elsewhere. So the average period of delay for most importers will come down to 4 weeks.





This brings me to the proposed 14th Directive. You really don't need to remind me of the strong UK support for this proposal, which I shall reaffirm in the House. Indeed I shall give an undertaking in my Budget Speech to reintroduce postponed accounting as and when the Community agrees to adopt it as the basis for harmonisation. This is an unconditional commitment. But I hope you will understand that the UK cannot indefinitely 'go-it-alone' while our major EC competitors retain VAT systems less biased in favour of imports than ours.

On other VAT changes, the extensions to the base are a crucial part of my policy of switching from taxes on income to taxes on spending. Any extension of VAT into areas that were previously relieved is bound to be highly sensitive politically. But the items I have chosen to tax were in fields where the case for continuing relief was least strong. You will undoubtedly be disappointed that I could not act on the zero-rated items which are in dispute between us. I am afraid that the Commission's failure so far to convince me of its case, combined with the political delicacy of the issues involved, means that we must continue to differ.

I have raised the VAT registration threshold in line with inflation since 1973, as I am persuaded that to do so is both in accordance with a proper interpretation of the Sixth Directive (and the ancillary statements recorded with its adoption) and right in principle in order to keep as many small traders as possible out of the VAT net. In the present economic circumstances I see no sense in stifling with bureaucracy the entrepreneurial spirit of the small business sector.

Turning now to the duties on alcoholic drinks, you will see that I have reduced the duty on wine and raised that on beer in order to comply fully with the European Court's judgement. The new ratio between the duties is just under 3 to 1 and accords with the requirements of article 95 of the Treaty; and I have neither restructured the wine duty nor attempted to phase the change over two or more Budgets. I am sure you will agree that my action is compatible with your proposals to revive discussion of harmonisation of excise duties on alcoholic beverages.

In changing the duties on drinks I have gone further. The rates of duty on made wine are now fully aligned with those on wine of fresh grapes, and cider containing between 8.5 and 8.7 per cent alcohol has been brought into the made wine category. There is now therefore no difference in the fiscal treatment of wine and made wine, and I trust the Commission will feel able to drop proceedings on this matter.

My officials are today going over the details of these changes with your people in DG XV. But I thought it right to tell you personally what lay behind my decisions.



SPARE.

BUDGET SECRET



CH/EX REF NO B(84)618

FROM: J O KERR

DATE: 12 March 1984

MR LOVELL

cc Financial Secretary  
Mr Monck

NISSAN

--- The Chancellor is content with the attached revised version of the draft telegram to Tokyo which you submitted on 9 March. No doubt it will now need re-clearance with your DTI contacts, and you may think it would be best for them to arrange its despatch, rather than for us to do so via FCO channels.

A handwritten signature in black ink, appearing to read 'J O Kerr'.

J O KERR



BUDGET SECRET

DRAFT TELEGRAM TO TOKYO

BUDGET CHANGES AND NISSAN

1. In his Budget Speech on 13 March the Chancellor will announce the phased withdrawal over 3 years of capital allowances - the first year allowance on plant and machinery and the initial allowance on buildings - but writing down allowances on these categories of capital expenditure will continue to be available; these changes will be offset by progressive reductions in the corporation tax rate from the current level of 52 per cent to 35 per cent in respect of profits earned in 1986-87.
2. The Chancellor will also announce in the Budget that, for regional policy reasons there will be transitional provisions, the effect of which will be to continue the current allowances for capital expenditure on all project in development areas and special development areas for which an offer of selective assistance has been made by Budget Day - 13 March 1984. These general transitional arrangements are to minimise any temporary difficulties for projects in the development of special development areas in recognition of the problems which these regions face.
3. These changes will in general lead to higher rental charges for leasing, the form of finance on which the Nissan projects will rely, since rental charges reflect the level of first year allowances. If the allowances are reduced, rental charges will rise. However since Nissan will be covered by these general transitional arrangements, the leasing rental charges in relation to the project's capital expenditure will not be adversely affected.



BUDGET SECRET

4. You will recall that the agreement with Nissan on 1 February 1984 included the letter, signed by the Secretary of State for Trade and Industry, confirming that "the Bank of England will use its good offices to assist Nissan in the arrangement of a leasing package if so requested". This letter reflected undertakings given personally by the Prime Minister to Mr Kawamata on the leasing question.

5. It will be important to re-assure Nissan immediately the Budget Statement has been made. You should therefore seek an interview with Ishihara (or, in his absence, with Kawamata) and speak to the following Aide Memoire. Nissan may find this confusing at first. It may be as well to leave with them a copy of the text.

"In the spirit of co-operation which has surrounded your important investment in the UK I have been asked, on the instructions of the Prime Minister, to explain the effects of certain changes in corporate taxation announced in the annual budget today (13 March) by the Chancellor of the Exchequer.

The important point from your point of view is that the announcement contained general transitional arrangements for certain projects in Development Areas and Special Development Areas. As the Nissan project will fall within these general regional policy arrangements, the tax changes will not affect it.

The principal changes involve the progressive withdrawal of capital allowances - the first year allowance on plant machinery and the initial allowance on buildings - leaving only writing down allowances, offset by progressive reduction in the rate of corporation tax from the current levels of 52 per cent to 35 per cent in respect of profits earned in 1986-87.



BUDGET SECRET

The transitional arrangements the Chancellor announced will have the following effects. The current rates of first year allowance on plant and machinery and initial allowances on industrial buildings will continue to apply to future capital expenditure which is incurred on a project in a development area or special development area in respect of which an offer of selective assistance has been made between 1 April 1980 to date (13 March, 1984) under Section 7 or 8 of the Industrial Development Act 1982 or the equivalent legislation in Northern Ireland. The purpose of these transitional arrangements is to minimise any temporary difficulties for projects in the development or special development areas in recognition of the problems which these regions face.

We are satisfied that with these transitional arrangements there will be no adverse impact from the tax changes on the Nissan project, and indeed in the longer run, particularly after phase 2, the reduction in corporation tax should have significant positive benefits."



Ch/Ex Ref No

B.(84)619



FROM: MISS M O'MARA

DATE: 12 MARCH 1984

PS/Economic Secretary

cc PS/Chief Secretary  
PS/Financial Secretary  
PS/Minister of State  
Sir P Middleton  
Sir T Burns  
Mr Cassell  
Mr Battishill  
Mr Evans  
Mr Lankester  
Mr Odling-Smee  
Mr Sedgwick  
Mrs Lomax  
Mr Riley  
Mr Mowl  
Mr Ridley

## THE BUDGET AND FINANCIAL FLOWS

The Chancellor has seen Mr Cassell's minutes of 9 March. He has enquired how the nationalised industries are affected by the CT package and has asked whether their EFLs should be adjusted. He would like urgent analysis and advice on this point.

msm

MISS M O'MARA



CONFIDENTIAL



FROM: J O KERR

DATE: 12 March 1984

MR UNWIN

cc Economic Secretary  
Sir P Middleton  
Mr Littler  
Mr Lavelle  
Mr Mountfield  
Mrs Case  
Mr Denison

ARGENTINA: COMMERCIAL BANK LOAN

The Chancellor has seen your minute of 9 March about the proposal that half of the outstanding \$1 billion commercial bank lending should not after all be made conditional on approval of an IMF programme, but should be releasable on the basis of a letter of intent approved by Larosiere. He does not like this proposal; and he thinks that you should make that clear to the Bank today, though he would be content for you also to make the points suggested in your paragraph 6.

*JOK*

J O KERR





CH/EX REF NO BC84622.

FROM: MISS M O'MARA

DATE: 12 March 1984

PS/FINANCIAL SECRETARY

cc PS/Chief Secretary  
PS/Minister of State  
PS/Economic Secretary  
Sir P Middleton  
Mr Bailey  
Mr Cassell  
Mr Monck  
Mr Battishill  
Mr Lovell  
Mr Monger  
Mr R I G Allen  
Mr Lord

PS/IR  
Mr Beighton - IR

Mr Graham - Parly Counsel

SHIPPING: MR RIDLEY'S LETTER OF 7 MARCH

The Chancellor has seen the Financial Secretary's suggestion that he might write to Mr Ridley (your minute of 9 March). He agrees and would be grateful if the Inland Revenue could submit a draft which he might send after the Budget.

*MOM*

MISS M O'MARA





Ch/Ex Ref No B(84) 621...

FROM: MISS M O'MARA  
DATE: 12 March 1984

Mr Taylor Thompson,  
Inland Revenue

cc PS/CST  
PS/EST  
PS/MST  
Mr Cassell  
Mr Monger  
Mr R I G Allen  
Mr Peretz  
Mr Lord  
PS/IR

CT PACKAGE: EFFECT ON DOUBLE TAX ARRANGEMENTS

The Chancellor was grateful for your note of 9 March. He would like the Financial Secretary to keep this aspect of the CT package under review.

*mom*

Miss M O'Mara





Ch/Ex Ref No **BC(E) 620**

FROM: MISS J C SIMPSON  
DATE: 12 March 1984

MR WALTON

cc PS/CST  
PS/FST  
PS/EST  
PS/MST  
Mr Cassell  
Mr Battishill  
Mr Monger  
Mr Folger  
Mr Griffiths  
Mr Ridley  
Mr Lord  
Mr Portillo  
Mr Knox, C & E

VAT BASE

The Chancellor has seen and was grateful for your further minute of 9 March.

*B*

Miss J C Simpson  
Private Secretary





Ch/Ex Ref No ... *B(84)634*

FROM: J O KERR  
DATE: 12 March 1984

Mr Monck

- cc PS/CST
- PS/FST
- PS/MST
- PS/EST
- Sir P Middleton
- Sir T Burns
- Mr Bailey
- Mr Cassell
- Mr Battishill
- Mr Monger
- Mr Folger
- Mr Norgrove
- Mr Ridley
- Mr Lord
- Mr Portillo
- PS:IR
- Mr Beighton: IR
- PS: C & E

BUDGET AIDE-MEMOIRE FOR THE CBI

The Chancellor was grateful for the draft text for the CBI which you submitted on 9 March.

2. I attach a re-typed version, incorporating his changes to paras 3, 7, 8, 14, 15 and 17.

3. You told me that arrangements for the delivery of the aide-memore to the CBI have already been made.

J O KERR



## BUDGET AIDE-MEMOIRE FOR THE CBI

The Budget set the Government's course for this Parliament. The MTF5 has been extended to cover 5 years. The Budget has two themes: to reduce inflation and improve the prospects for jobs; and to reform and simplify the tax system in a way that improves economic performance.

The PSBR and interest rates

2. For 1984/85 the Budget is revenue neutral. It will reduce the PSBR sharply as a percentage of GDP and this should allow progress to lower interest rates to be resumed. For 1985/86 the tax measures will have a revenue cost of about £1½ billion. There are no public expenditure measures.

Business tax burden cut over next two years

3. The Budget measures directly affecting business will reduce its tax burden over the next two years taken together by about £900 million, compared with an indexed base. In 1984/85 alone, within a neutral Budget, business will pay up to £500 million more tax (entirely as a result of the earlier payment of VAT on imports) but this will be outweighed by the gain to business in 1985/86 of about £1400 million. In the longer term the reduction in corporation tax rates to 35 per cent will give a lasting cut in the tax burden on business.

Major business tax measures

4. The major measures include:
- a. corporation tax reform: abolition of stock relief; phasing out first year capital allowances; and reducing the CT rate by stages from 52 per cent to 35 per cent. The CT rate for small companies comes down immediately from 38 per cent to 30 per cent. The result will be broadly that UK capital allowances will move into line with those in other countries and corporation tax rates will be lower;



- b. early payment (on average a month after entry) for VAT on imports from 1 October, which will improve the competitiveness of UK producers against imports;
- c. abolition of NIS from 1 October;
- d. halving the rate of Stamp Duty from 2 per cent to 1 per cent.

... The Finance Bill will embody all these changes so that business will be able to plan with confidence. The attached press notice explains the purpose and effects of (a) and (c) in more detail. In brief, the measures will raise profits after tax by lightening the tax burden and reduce the distortions entrenched in the present system. Businesses will be able to spend more on innovation of all kinds; and investment will be higher quality and bring a higher pre-tax return to the economy.

#### Business and the capital market

- 5. The halving of Stamp Duty should lead to increased trading in equities and to more purchases by individuals. This should make it easier and cheaper for companies to raise new equity.
- 6. The Budget also contains measures which will benefit company stock issues: the new arrangements for deep discount stock and reliefs for companies issuing euro-bonds and convertible loan stock announced last year will go ahead: and new corporate fixed interest securities held for more than a year will now be exempt from CGT.

#### Indirect taxes

- 7. As part of a switch from taxes on earnings to taxes on spending, VAT will be extended to 2 areas at present zero-rated - alterations to buildings, and hot take-away food and drink - and tobacco duty is being increased by 15 per cent.



8. Most other excise duties, and vehicle excise duty, will go up roughly in line with prices. Heavy oil duty will not be raised, and kerosene duty will be abolished.

9. The VAT registration threshold is raised to £18,700, as much as the EC directive allows.

#### Direct personal taxes

10. The relief for foreign earnings will be withdrawn for residents who spend between 30 and 365 days abroad.

11. Benefit scales for cars and for fuel provided by employers will be raised by 10 per cent with effect from April 1985.

12. There will be a number of changes in capital taxes, which will help small businesses. The higher rate of Capital Transfer Tax will be cut from 75 per cent to 60 per cent. For lifetime gifts the rate will be half the rate on death over the whole scale. The limit for retirement relief for CGT will be doubled. The DLT threshold will be raised from £50,000 to £75,000.

13. The Investment Income Surcharge will be abolished.

14. There will be no change in income tax rates. Most allowances and tax thresholds will go up in line with prices. But in order to ease the poverty and unemployment traps the basic threshold will rise by 12½ per cent, well over double the rise in prices. Every tax paying married couple of working age will have a tax cut of at least £2 a week.

15. Two changes will encourage share options. The contribution ceiling for savings-related share option schemes will be doubled from £50 to £100 a month. Secondly in order to do more to make top quality company management mobile and to increase the incentives to existing executives, share options generally, subject to certain limits and conditions, will be taken out of income tax altogether. Any gain will be subject to CGT on ultimate disposal.



Conclusion

16. The Budget will bring business substantial benefits. The effect of the tax changes, particularly of the CT reforms and early payment of VAT on imports, on individual companies will of course vary widely. But the overall tax burden on business will be lightened over the next two years by nearly £1 billion. In the longer term the cut in the Corporation Tax rate by a third to 35 per cent, which will be in this year's Finance Bill, will mean a lasting reduction in the tax burden. The abolition of NIS will benefit all employers, improving competitiveness, and the prospect for jobs. The cut in the PSBR should bring down interest rates and tax changes will make companies' access to capital markets cheaper. The wider scope for stock options will help to improve the mobility of key managers and to innovate and reward those who do not change jobs for good performance. More generally the tax reform will help to improve the UK's economic performance.

17. Small businesses will gain from the capital tax changes and in particular from the immediate reduction in the small companies CT rate from 38 per cent to 30 per cent, well below the rate in most other countries.



CH/EX REF NO BC84/627

FROM: MISS M O'MARA

DATE: 12 March 1984

MR MACE - Inland Revenue

cc PS/Chief Secretary  
PS/Financial Secretary  
PS/Minister of State  
PS/Economic Secretary  
Sir P Middleton  
Sir T Burns  
Mr Cassell  
Mr Battishill  
Mr Monger  
Mr Watson  
Mr Folger  
Ms Seammen  
Mr Allen  
Miss Noble  
Mr Martin  
Mr Aaronson  
Mr Ridley  
Mr Lord  
Mr Portillo

## BUDGET INCOME TAX CHANGES AND HOUSING BENEFIT

The Chancellor has seen your minute of 9 March. He has commented that it is for Mr Fowler to make the running on this subject rather than Treasury Ministers but he has noted that the fact that about 80 per cent of working HB losers will have cash income tax gains greater than their HB losses (your paragraph 9) is quite a useful point.

*Mom*

MISS M O'MARA



CH/EX REF. NO. B(81)618



FROM: MISS J C SIMPSON

DATE: 12 March 1984

cc PS/Chief Secretary  
PS/Financial Secretary  
PS/Minister of State  
PS/Economic Secretary  
Sir P Middleton  
Mr Cassell  
Mr Battishill  
Mr Folger  
Mr Allan  
Mr Reed  
Mr Painter - IR

MR MONGER

**ACTION FROM 1 MARCH MEETING**

The Chancellor has seen the notes attached to your minute of 9 March.

2. On the note on the cost of the CT package, he has asked that the suggested line to take in the penultimate sentence of paragraph 5 be checked against the Budget speech.

2. On the question of the self employed, he has assumed that the reference to their being substantial net losers refers to the unincorporated self employed. He would like to know what percentage of the total self employed these comprise, and he would also be grateful for suggestions about what might be done to help them specifically in a future Budget.

J

MISS J C SIMPSON





FROM: J O KERR  
DATE: 12 March 1984

Ch/Ex Ref No B.(84)637.

Mr Monck

cc PS/CST  
PS/FST  
PS/MST  
PS/EST  
Sir P Middleton  
Sir T Burns  
Mr Bailey  
Mr Cassell  
Mr Battishill  
Mr Monger  
Mr Folger  
Mr Norgrove  
Mr Ridley  
Mr Lord  
Mr Portillo  
  
PS/IR  
Mr Beighton/IR  
PS/C & E

BUDGET AIDE-MEMOIRE FOR THE CBI

The Chancellor has now seen the Financial Secretary's comments on the paper for the CBI, and agrees to two changes to the version which I sent to you this morning.

- (a) para 3, line 5 - for "entirely" read "solely";
- (b) para 12, line 2 - for "small businesses" read "family businesses".

A handwritten signature in black ink, appearing to be 'J O KERR'.

J O KERR





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

12 March 1984

The Rt Hon James Prior MP  
Secretary of State for Northern Ireland  
Northern Ireland Office

A handwritten signature in black ink, appearing to read 'James Prior'.

TOBACCO DUTY

My reply a month ago to your letter of 25 January about tobacco duty was necessarily rather uninformative. But I think it right now to give you advance warning of the fact that I shall tomorrow be proposing in the House a fairly steep rise in tobacco duty.

The point which most concerned you was, of course, the implications for the Province of large increases in the duty on pipe tobacco. With this in mind, I have managed to get away with no increase whatsoever for the pipe-smoker. I hope that you will think this a pretty fair deal under the circumstances.

A handwritten signature in black ink, appearing to read 'Nigel Lawson'.

NIGEL LAWSON



Ref No. 3(84) 647.

BUDGET SECRET



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

12 March 1984

Andrew Turnbull Esq  
10 Downing Street

*Dear Andrew,*

BUDGET SPEECH

- .. I attach the final version of the Chancellor's Speech tomorrow. You will see that it has got still better!

*Yours ever,*

*JOK*  
J O KERR



CH/EX REF NO B(84)648

FROM: MISS J C SIMPSON

DATE: 12 March 1984

MR R I G ALLEN

cc PS/Chief Secretary  
PS/Financial Secretary  
PS/Minister of State  
PS/Economic Secretary  
Sir P Middleton  
Mr Monck  
Mr Battishill  
Mr Monger  
Mr Lovell  
Mr Folger  
Mr Norgrove  
Mr Ridley  
Mr Lord  
Mr Portillo

PS/IR  
Mr Beighton - IR  
Mr McConnachie - IR

TREASURY PRESS RELEASE: THE BUDGET: BUSINESS AND TAX REFORM

This is to confirm what I told you earlier today on the telephone that the Chancellor is content with the additional paragraph contained in your minute of 12 March, subject to the deletion of "more" in the middle of line 6. I also told you that the Chancellor would prefer, if possible, not to specify "medium life" but to use wording closer to that of the Budget Speech. You agreed to see if amendments taking on both these points were possible.

*J*

MISS J C SIMPSON



12 MAR 1984

BUDGET SECRET



*fu*

FROM: A P HUDSON  
DATE: 12 March 1984

PS/CHANCELLOR

cc Chief Secretary  
Minister of State  
Economic Secretary  
Sir P Middleton  
Mr Monck  
Mr Cassell  
Mr Battishill  
Mr Monger  
Mr Allen  
Mr Folger  
Mr Ridley  
Mr Lord  
Mr Portillo  
PS/IR  
PS/C&E

BUDGET AIDE-MEMOIRE FOR THE CBI

1. The Financial Secretary has seen the draft attached to Mr Monck's 9 March minute.
2. In paragraph 12, he would omit the phrase "which would help small businesses".
3. More importantly, he thinks that paragraph 3 in its present form will be an own goal. He is aware of all the debates on VAT and imports and the Budget balance. But in an aide-memoire for the CBI, he thinks it would be very unwise not to bring out the one-off nature of VAT on imports, and its actual effect on corporations, as oppose to the banking system. This could be done by illustrating that, if one is looking only at corporations, the effect is at interest charge. Including it as a negative in the effect of the Budget on companies over the years 1984-85 and 1985-86 does not bring this out.

*APH*

A P HUDSON



12 MAR 1984

BUDGET SECRET



Ch/Ex Ref No

.....B(84)634

FROM: J O KERR

DATE: 12 March 1984

Mr Monck

cc PS/CST  
PS/FST  
PS/MST  
PS/EST  
Sir P Middleton  
Sir T Burns  
Mr Bailey  
Mr Cassell  
Mr Battishill  
Mr Monger  
Mr Folger  
Mr Norgrove  
Mr Ridley  
Mr Lord  
Mr Portillo  
PS:IR  
Mr Beighton: IR  
PS: C & E

BUDGET AIDE-MEMOIRE FOR THE CBI

The Chancellor was grateful for the draft text for the CBI which you submitted on 9 March.

2. I attach a re-typed version, incorporating his changes to paras 3, 7, 8, 14, 15 and 17.
3. You told me that arrangements for the delivery of the aide-memore to the CBI have already been made.

A handwritten signature in black ink, appearing to read 'J O Kerr'.

J O KERR

BUDGET SECRET



## BUDGET AIDE-MEMOIRE FOR THE CBI

The Budget set the Government's course for this Parliament. The MTFS has been extended to cover 5 years. The Budget has two themes: to reduce inflation and improve the prospects for jobs; and to reform and simplify the tax system in a way that improves economic performance.

The PSBR and interest rates

2. For 1984/85 the Budget is revenue neutral. It will reduce the PSBR sharply as a percentage of GDP and this should allow progress to lower interest rates to be resumed. For 1985/86 the tax measures will have a revenue cost of about £1½ billion. There are no public expenditure measures.

Business tax burden cut over next two years

3. The Budget measures directly affecting business will reduce its tax burden over the next two years taken together by about £900 million, compared with an indexed base. In 1984/85 alone, within a neutral Budget, business will pay up to £500 million more tax (entirely as a result of the earlier payment of VAT on imports) but this will be outweighed by the gain to business in 1985/86 of about £1400 million. In the longer term the reduction in corporation tax rates to 35 per cent will give a lasting cut in the tax burden on business.

Major business tax measures

4. The major measures include:
- a. corporation tax reform: abolition of stock relief; phasing out first year capital allowances; and reducing the CT rate by stages from 52 per cent to 35 per cent. The CT rate for small companies comes down immediately from 38 per cent to 30 per cent. The result will be broadly that UK capital allowances will move into line with those in other countries and corporation tax rates will be lower;



- b. early payment (on average a month after entry) for VAT on imports from 1 October, which will improve the competitiveness of UK producers against imports;
- c. abolition of NIS from 1 October;
- d. halving the rate of Stamp Duty from 2 per cent to 1 per cent.

... The Finance Bill will embody all these changes so that business will be able to plan with confidence. The attached press notice explains the purpose and effects of (a) and (c) in more detail. In brief, the measures will raise profits after tax by lightening the tax burden and reduce the distortions entrenched in the present system. Businesses will be able to spend more on innovation of all kinds; and investment will be higher quality and bring a higher pre-tax return to the economy.

#### Business and the capital market

5. The halving of Stamp Duty should lead to increased trading in equities and to more purchases by individuals. This should make it easier and cheaper for companies to raise new equity.

6. The Budget also contains measures which will benefit company stock issues: the new arrangements for deep discount stock and reliefs for companies issuing euro-bonds and convertible loan stock announced last year will go ahead: and new corporate fixed interest securities held for more than a year will now be exempt from CGT.

#### Indirect taxes

7. As part of a switch from taxes on earnings to taxes on spending, VAT will be extended to 2 areas at present zero-rated - alterations to buildings, and hot take-away food and drink - and tobacco duty is being increased by 15 per cent.



8. Most other excise duties, and vehicle excise duty, will go up roughly in line with prices. Heavy oil duty will not be raised, and kerosene duty will be abolished.

9. The VAT registration threshold is raised to £18,700, as much as the EC directive allows.

#### Direct personal taxes

10. The relief for foreign earnings will be withdrawn for residents who spend between 30 and 365 days abroad.

11. Benefit scales for cars and for fuel provided by employers will be raised by 10 per cent with effect from April 1985.

12. There will be a number of changes in capital taxes, which will help small businesses. The higher rate of Capital Transfer Tax will be cut from 75 per cent to 60 per cent. For lifetime gifts the rate will be half the rate on death over the whole scale. The limit for retirement relief for CGT will be doubled. The DLT threshold will be raised from £50,000 to £75,000.

13. The Investment Income Surcharge will be abolished.

14. There will be no change in income tax rates. Most allowances and tax thresholds will go up in line with prices. But in order to ease the poverty and unemployment traps the basic threshold will rise by 12½ per cent, well over double the rise in prices. Every tax paying married couple of working age will have a tax cut of at least £2 a week.

15. Two changes will encourage share options. The contribution ceiling for savings-related share option schemes will be doubled from £50 to £100 a month. Secondly in order to do more to make top quality company management mobile and to increase the incentives to existing executives, share options generally, subject to certain limits and conditions, will be taken out of income tax altogether. Any gain will be subject to CGT on ultimate disposal.



Conclusion

16. The Budget will bring business substantial benefits. The effect of the tax changes, particularly of the CT reforms and early payment of VAT on imports, on individual companies will of course vary widely. But the overall tax burden on business will be lightened over the next two years by nearly £1 billion. In the longer term the cut in the Corporation Tax rate by a third to 35 per cent, which will be in this year's Finance Bill, will mean a lasting reduction in the tax burden. The abolition of NIS will benefit all employers, improving competitiveness, and the prospect for jobs. The cut in the PSBR should bring down interest rates and tax changes will make companies' access to capital markets cheaper. The wider scope for stock options will help to improve the mobility of key managers and to innovate and reward those who do not change jobs for good performance. More generally the tax reform will help to improve the UK's economic performance.

17. Small businesses will gain from the capital tax changes and in particular from the immediate reduction in the small companies CT rate from 38 per cent to 30 per cent, well below the rate in most other countries.



12 MAR 1984

BUDGET SECRET

*file*



FROM: J O KERR  
DATE: 12 March 1984

Ch/Ex Ref No B.(84)637.

Mr Monck

cc PS/CST  
PS/FST  
PS/MST  
PS/EST  
Sir P Middleton  
Sir T Burns  
Mr Bailey  
Mr Cassell  
Mr Battishill  
Mr Monger  
Mr Folger  
Mr Norgrove  
Mr Ridley  
Mr Lord  
Mr Portillo  
  
PS/IR  
Mr Beighton/IR  
PS/C & E

BUDGET AIDE-MEMOIRE FOR THE CBI

The Chancellor has now seen the Financial Secretary's comments on the paper for the CBI, and agrees to two changes to the version which I sent to you this morning.

- (a) para 3, line 5 - for "entirely" read "solely";
- (b) para 12, line 2 - for "small businesses" read "family businesses".

*JOK.*

J O KERR

BUDGET SECRET

50



CH/EX REF. NO. B(652)84

FROM: MISS J C SIMPSON

DATE: 13 March 1984

cc PS/Chief Secretary  
PS/Financial Secretary  
PS/Minister of State  
PS/Economic Secretary  
Mr Battishill  
Mr Monger  
Mr Griffiths  
PS/C&E

MR JEFFERSON SMITH - CUSTOMS AND EXCISE

**VAT EXTENSIONS**

The Chancellor has seen your minute to me of 12 March and was grateful.

*B*

MISS J C SIMPSON



CH/EX REF. NO. B(653)84

FROM: MISS J C SIMPSON

DATE: 13 March 1984

cc PS/Chief Secretary  
PS/Financial Secretary  
PS/Minister of State  
PS/Economic Secretary  
Sir P Middleton  
Mr Littler  
Mr Cassell  
Mr Monger  
Mr Battishill  
Mr Griffiths  
Mr Norgrove  
Mr Folger

MR KNOX - CUSTOMS AND EXCISE

**VERMOUTH**

The Chancellor has seen your minute of 12 March, with advice on the acceptability of the letter from Pandolfi conveyed in telegram number 157.

2. He is content with your proposal that MAFF officials and yourself should reply to any immediate enquiries about the details of the Italian undertaking by saying that no details were available for publication.
3. He has also commented that it is essential for us to keep the Vermouth surcharge as a possible further enducement to make the deal stick; the UK must keep up the pressure on the Italians in every way possible over the next few days.
4. The Chancellor has also seen Mr Freedman's minute of 12 March with the proposal for conveying to the Italian Government the Budget changes on wine and beer duties. This is to confirm that, as I told Mr Freedman this morning, the Chancellor is content with his proposals.

JJ

MISS J C SIMPSON



CH/EX REF. NO. B(651)84

FROM: MISS J C SIMPSON

DATE: 13 March 1984

cc Sir P Middleton  
Mr Littler  
Mr Battishill  
Mr Monger

MR NORGROVE

**GUIDANCE TELEGRAM FOR OVERSEAS POSTS**

This is to confirm that the Chancellor is content with the telegram attached to your minute of 12 March.

B

MISS J C SIMPSON



CH/EX REF. NO. 1 (84) 649.

FROM: MISS M O'MARA

DATE: 13 March 1984

cc *PS/ Financial Secretary*  
Sir P Middleton  
Mr Bailey  
Mr Anson  
Mr Monck  
Mr Burgner

MR ROBSON

**WYTCH FARM**

The Chancellor has seen Sir Kenneth Couzens' letter of 12 March. He has commented that in his own judgement, this is a matter for BGC; it is not for the Government to make suggestions. However, if BGC do ask for guidance, he believes that the Department of Energy should use their good offices to seek an early and equitable resolution of the issue. If it is clear that the Corporation are dragging their feet, he believes the 1982 Act will need to be invoked. But he has added that morally, at the end of the day the sale should still be to the Dorset Group, although we need not indicate that this is our view at this stage.

*MOM*

MISS M O'MARA



Ch/Ex Ref No. B(84)162



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

PRIME MINISTER

I owe you a report on the changes in the excise duties which I envisage for the Budget.

2. I am sure that it is right to aim at broad revalorisation: this is what people have come to expect, and the RPI impact effect is small, given low inflation. But I propose a number of minor exceptions.
3. The most politically sensitive items are of course petrol and derv. For petrol, I have in mind an increase of 4.5p a gallon, exactly what is required by revalorisation, but on derv I propose an increase of only 3.5p a gallon, which is a slight rounding down of the strict revalorisation increase (3.8p). I have consulted Nick Ridley, Peter Walker, George Younger, Nick Edwards, and John Wakeham: all are content, with my plans. (But I might of course still have to review them again if our forecast, or the outlook for crude oil prices, were to change significantly before the Budget.)
4. As to tobacco, I have in mind an increase of 4p for 20 cigarettes. This is a rounding up of the straight revalorisation increase of 3.5p. As a minor concession, sought by Jim Prior, because of the industrial implications in Northern Ireland, there would be no increase in the duty on pipe tobacco.
5. On the Vehicle Excise duty, straight revalorisation of the £85 rate for cars and light vans would produce £89.50, but





Nick Ridley and I have agreed that this should be rounded up to £90. We have also agreed changes in VED on goods vehicles which will produce very slightly (£3m) more than revalorisation. The duty for most goods vehicles will in fact rise broadly in line with revalorisation but there will be reductions for the lightest lorries offset by higher increases for some heavier lorries, to recognise their differing contribution to road costs.

6. Finally, drinks. After consultation with Geoffrey Howe about the recent European Court judgement, I propose an increase in the duty on beer of 2p a pint, and a reduction in the duty on wine of about 18p a bottle. Following the unsatisfactory talks which Michael Jopling and I had in Rome with our Italian counterparts over the Italian foot-dragging on the implementation of the analogous European Court judgement against their discrimination against Scotch whisky, I am in touch with Geoffrey Howe about the possibility of a temporary surcharge on vermouth, to put pressure on them. On other drinks, I have in mind an increase of 10p a bottle for spirits - well below revalorisation - 10p a bottle for fortified wines, and 3p a pint for cider.

7. I have in mind one other small concession: abolition, at a cost of only £5m, of the 1p a gallon duty on kerosene, which applies to paraffin used, mainly by the elderly, for home heating.

8. Altogether these increases will yield about £660m in a full year, compared to £640m from strict revalorisation. The RPI impact effect will be only 0.4 per cent, and this has of course already been allowed for in our forecast.

9. I see no serious problems here, but I would be grateful to know whether you too would be content with the proposed changes. I would of course consult you again if I had to consider larger increases for petrol and derv; and I shall let you know in due course what conclusions Geoffrey and I reach about vermouth.

N.L.

16 February 1984





FST.

S.R.P. MIDDLETON.

MR CASSELL.

MR MONCK.

MR BURNIER.

MR S A ROBSON.

MR WOOD, MR JOHNS (CR).

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

PRIME MINISTER

**NORTH SEA FISCAL REGIME**

I promised last week that I would let you have details of my Budget proposals for the North Sea fiscal regime, once I had discussed them with Peter Walker.

2. As in previous years, officials of the Treasury, Inland Revenue and Department of Energy have carried out a detailed analysis of UKCS oil and gas projects. In the light of this, I have concluded that, overall, the present fiscal regime is about right. The renewed interest shown in North Sea projects since the last Budget seems to bear out this judgement. In a later year we may need to look again at the taxation of Southern Basin gas fields but I propose no change in this area now.

3. I do intend to announce certain changes directed at reducing the tax incentives for the sale of licence interests (so called "farmouts") of which BP's disposal of part of its interest in the Forties field provides a recent example. My proposals are quite modest and should have no adverse impact on deals that have a genuine commercial motivation rather than tax avoidance. The measures I propose are:

- (i) removing a loophole which lets out of charge to capital gains tax gains by non-residents on tangible assets used in the North Sea. This is a clear anomaly;
- (ii) bringing capital gains tax on farmouts within the corporation tax ring-fence; and
- (iii) limiting the buyer's capital allowances for plant and machinery in a farmout to the seller's original cost.





4. I have also examined the implications for North Sea developments of my wider proposals on corporation tax. North Sea companies will gain substantially from these, particularly the existing fields. As I see no reason to relax the present fiscal regime in the North Sea, this implies that these gains should be at least partially offset. I do not want to raise the rate of PRT. Instead I intend to stop the repayment of ACT which is presently allowed when corporation tax liabilities are reduced as a result of PRT deductions. This measure should not affect development. It goes a considerable way to offsetting the gains in the North Sea from the wider corporation tax package, but a net benefit will remain.
5. Taken together these proposals will, on our latest forecasts, reduce Exchequer revenue from the North Sea by on average about £55 million a year over the next five years. The marginal rate of take on existing fields will fall from 89.5 per cent to 85.8 per cent, and on future fields (which are not liable to royalty) from 88 per cent to 83.75 per cent.
6. This leaves the problem of incremental projects in existing fields which have an important role to play in the full exploitation of the UKCS. The industry has expressed concern for some time about the impact of the present fiscal regime on such projects and the general corporation tax package will exacerbate their relative disadvantage. I believe we must give some concessions in this area, but we shall need to consult with the industry in order to identify the best options. We cannot open discussions before the Budget and so have no hope of completing consultation in time for this year's Finance Bill.
7. However, I shall be announcing in the Budget my plans for consultation with the industry and shall give an undertaking to legislate next year to improve the position of incrementals. To guard against the risk that this approach could lead to projects being deferred, I will make plain that concessions will be backdated to this year.
8. I have discussed my proposals with Peter Walker, to whom I am sending a copy of this minute. He is content.

A handwritten signature in dark ink, appearing to be 'N.L.', written in a cursive style.

(N.L.)

2 March 1984





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

*PT*  
Sir P. Middleton  
Mr Bathshill

PRIME MINISTER

**BUDGET: TAX REFORM**

You already have my Budget proposals on the MTFs, on the Excise Duties, and on the reform of Business taxation. This minute covers my remaining tax proposals, and in particular the two further areas in which I envisage major reform, ie changes in the balance of taxation on income and on expenditure, and changes in the area of savings and investment to increase the role of individuals.

Shifting the balance

2. I am sure it is right to shift when and where we can to taxing spending rather than earning. It is not simply a matter of increasing individual freedom to spend or save: only by cutting income tax can we tackle the poverty and unemployment traps, and maintain the momentum of improving incentives.

3. I do not believe that the right route is a further increase in the VAT rate; my preference is for widening the VAT base, which at present covers little more than half of consumers' expenditure. As you know, there are three areas where I believe we can, and should, extend the base. These are:-

(a) newspapers, periodicals, newspaper advertisements and news services. There is no case on merit for leaving these untaxed. Nor, in logic, is there a case for not applying VAT to books, but I have decided against bringing them in.

(b) building alterations and extensions. The present position, with necessary maintenance and repairs attracting VAT, but alterations and extensions not doing so, is manifestly absurd.

(c) hot take-away food. By this I mean hamburgers and other fast food products, fish and chips, Chinese take-away meals etc. It makes no sense that the fast food restaurants now have two price-lists, one including VAT for those





who will do their eating on the premises, another, without VAT, for those who carry their purchases away. VAT is, of course, already levied on ice-cream, confectionery, chocolate, crisps etc.

These changes will raise an extra £600 million or so next year, and over £1 billion in 1985-86 - £340 million on newspapers etc, £490 million on alterations, and £220 million on take-away food. The effect on the RPI will be less than one-half of one per cent, so there is no threat to the counter inflation policy: inflation this year is still expected to be on a declining path.

4. In addition, as a surrogate for VAT - which the EC rules do not allow us to apply to financial services - I envisage a new licence duty on consumer and other forms of personal credit. An effective system of taxing the banks is long overdue. The new duty would be charged on a six monthly basis on outstanding credit issued, but would not be applied to loans made to businesses or to mortgages qualifying for income tax relief. I envisage a rate of 1 per cent. To allow time for preparation, it would apply only from July 1985, raising some £90 million in 1985-86, and some £200 million in a full year.

5. Given the extra money from VAT, it is already clear that, within the context of a neutral Budget, I can this year increase the single income tax allowance by £200 and the married allowance by £300. That is an 11 per cent increase, slightly more than double the amount required by indexation, and will particularly help the low paid. I am considering whether there is any way in which I could go a little further, in order to ensure that every married couple paying income tax gains - NIC apart - by at least £2 a week. There would be considerable attractions in that. The higher rate threshold, and the higher rate bands, would be fully revalorised but no more, as would the age allowance. (The higher paid of course get the largest cash gains from raising the allowances).

6. I should also mention that I have decided to sweep away two small out-dated reliefs: the relief on foreign earnings for those who spend 30 days or more working abroad, and (with suitable staging) the relief for foreigners coming here to work for foreign employers. Both date from the days of confiscatory top rates of income tax and have outlived their justification, and both are subject to substantial abuse. I must





also announce the 1985-86 car benefit scales for those who have company cars. We have been slowly increasing these to more realistic levels in recent Budgets. The increase last year was 15 per cent, but, with lower inflation, I plan to hold it to 10 per cent this time.

7. I also propose to make the tax treatment of executive share option schemes markedly more generous, along the lines we discussed before Christmas. The essence of my proposals is that gains under such schemes would in future be subject to Capital Gains Tax rather than (as at present) to income tax. This improvement, which has long been pressed upon us, will be widely welcomed, especially by smaller companies, who will now be able to attract key staff by the promise of substantial rewards.

8. The overall effect of this shift in the balance of direct and indirect taxation should be generally welcome. We have good news for the building trade, eg on Stamp Duty (para 12 below) and DLT (the threshold for which I envisage raising from £50,000 to £75,000, thus reducing by a third the number of cases it affects), and this will cushion the blow of VAT alterations. But I have no illusions about Fleet Street's likely reaction to the change affecting them. It may indeed colour their attitude to the whole Budget, but I am sure that it is right, and should not be ducked on that account.

#### Savings and investment

9. As you know, I believe that we must also make a start in removing some of the features of the tax system which distort the pattern of personal savings. I have three aims in mind:-

(a) to reduce the extensive privileges for institutional savings and make it more attractive for individuals to invest directly in equities;

(b) more generally, to increase the encouragement given to personal savings; and

(c) to put the banks and building societies on to a more equal footing.





10. First, I have reviewed the array of tax privileges which are putting more and more personal savings into the hands of the institutions and driving the direct investor out of equities. This is a classical case of reliefs and exemptions eroding the tax base and keeping income tax rates higher than they need be. It is something we have been concerned about for a very long time, and which our friends constantly urge us to tackle.

11. We cannot touch the tax treatment of pensions until Norman Fowler has completed his enquiry. But we can act now on life assurance premium relief. Relief from higher rates of tax was removed some years ago, but the allowance (at half the basic rate on qualifying premiums) still costs £700 million a year, is growing, and has been subject to considerable abuse in recent years. So I have concluded that the time has come to withdraw relief on new policies taken out after Budget Day. There is a strong case for gradually phasing out relief on existing policies as well; but to avoid any possibility of hardship, I propose to leave these completely untouched.

12. At the same time I propose to encourage investment in equities by halving the rate of Stamp Duty from 2 per cent to 1 per cent, which will help to strengthen the London market against growing US competition. I intend the cut also to apply to sales of houses and land, which will help housebuyers and the construction industry, and to raise the stamp duty threshold from £25,000 to £30,000, which will mean that 90 per cent of first-time buyers will not have to pay Stamp Duty at all.

13. Secondly, direct encouragement to personal savings. I see no justification whatsoever for continuing to tax savings income more heavily than earnings, and I propose to abolish the Investment Income Surcharge. Of course, our opponents will represent this as a hand-out to the rich; but half those liable to the surcharge are elderly, and many are by no means well-off. And the criticism is one which we shall have to face whenever we remove the surcharge - as we certainly must. I think it best to do it straight away, in the first Budget of the new Parliament.

14. In a broadly neutral Budget, I do not have room for substantial cuts in the capital taxes: we shall in any case be reviewing them, with Arthur Cockfield's help, before next year. But there are some small but useful changes which can be made now at modest cost. In particular, I have in mind to cut the top rate of capital transfer tax from 75 per cent to 60 per cent.





15. Finally, the banks and building societies. The banks have long complained of the unfair advantage enjoyed by the building societies by virtue of the composite rate, and campaigned for its abolition. But the composite rate is a sensible arrangement which simplifies tax return-filling, and saves large numbers of Revenue staff. So instead of taking it away from the building societies, I propose instead to extend it to the banks as well. This will eventually save 750-1000 Revenue staff, and demonstrates our willingness to encourage the movement towards interest on current accounts. The banks have been informed and don't like it; but their case is weakened by their having for so long complained that the composite rate gave the societies a competitive edge. And the fact that the new arrangements will not apply to deposits by foreign residents (or, of course, businesses) will help to meet fears of loss of overseas business. The banks will need a year to prepare: the new arrangements will not therefore apply until 1985-86.

16. The banks may to some extent be mollified by the fact that building society gains on gilts transactions will, as you know, be taxed in future on the same basis as gains by the banks. But it must be admitted that the effect of the composite rate on the banks may well be to cause upwards of £1 billion of bank deposits to be switched to the building societies in 1985-86, and we can expect them to object strongly to the change.

#### Summary

17. I enclose a table setting out all the main measures proposed (with the exception of North Sea taxation, for I still have to discuss with Peter Walker some possible ACT changes). The net effect is roughly neutral in 1984-85, but they reduce taxes by about £1.5 billion in 1985-86. Most of the extra second year benefit goes to business, but provided we stick to our published plans for public expenditure, the 1985-86 fiscal prospect still leaves room for substantial income tax cuts in next year's Budget.

18. The measures proposed for this year will mean we make a real start on reforming the tax system and getting the supply performance of the economy moving. There will be gainers and losers, as is inevitable in any radical change, and it will be vital to get the presentation right. But the story will be a good one, and I am determined that it should be well told.

N.L.

21 February 1984



BUDGET SECRET  
Provisional Costing of Proposed Changes

		£m*			
		1984-85		1985-86	
		-	+	-	+
<b>A</b>	<b><u>Income and Spending</u></b>				
1.	Excise duties (see 16 February minute)		10		10
2.	VAT on newspapers etc; alterations; hot take-away food		610		1050
3.	Consumer Credit Duty				90
4.	Withdraw reliefs on foreign earnings and foreign emoluments		42		65
5.	Car benefit scales for 1985-86				30
6.	Income tax thresholds etc**	700		860	
<b>B</b>	<b><u>Businesses</u></b> (see 16 February minute)				
7.	Corporation tax reform				
	- abolish stock relief and reduce first year capital allowances				750
	- offset by reducing main CT rate to 50 per cent in 1984-85 and to 45 per cent in 1985-86	200		1050	
	- and small companies CT rate to 30 per cent	80		150	
8.	VAT on imports (PAS)		1200		
9.	Abolish NIS from 1 August 1984	465		925	
<b>C</b>	<b><u>Savings and Investment</u></b>				
10.	Composite Rate on banks		neg		neg
11.	Life Assurance relief		90		240
12.	Halve Stamp Duty on share transfers	160		155	
13.	Halve Stamp Duty on land and buildings	290		360	
14.	Improve Share Options schemes			30	
15.	Capital Taxes				
	- CTT changes	3		7	
	- DLT threshold	1		5	
16.	Abolish IIS	25		210	

\*All figures are over and above the cost/yield from indexation

\*\*Assumes double-indexation of basic threshold



Undisclosed copies:

Sir P Middleton  
Sir T Burns  
Mr Cassell  
Mr Battishill

PRIME MINISTER

**MEDIUM TERM FINANCIAL STRATEGY**

The key to sustained recovery remains keeping inflation down, which in turn means further firm control of money supply growth, and of borrowing. So I plan to emphasise on 13 March the continuity of our economic policies, and to restate the Medium Term Financial Strategy, which, as Cabinet agreed on 9 February, will be extended to cover the next five years.

2. I shall of course be announcing monetary ranges for 1984-85. As you know, I have reviewed the formulation of monetary policy, and the results were foreshadowed in my Mansion House speech in October. I am sure that it is right now to have separate targets, consistent with a continuing reduction in inflation, for broad and narrow money, and the MTFS will therefore show ranges for £M3 and MO. There is no reason to change the range of 6-10 per cent for £M3 shown for 1984/85 in the 1983 MTFS. For MO (mainly notes and coin in the hands of the public) a range of 4-8 per cent would be appropriate. I envisage a subordinate role for PSL2 and M2 as cross checks on growth of broad and narrow money respectively. These changes were discussed with Alan Walters when he was last over; he was very much in favour of the new range for narrow money. For later years the MTFS will include illustrative ranges showing a downward path for both money measures, and making clear our determination to achieve a substantial reduction in monetary growth, taking us towards the ultimate objective of stable prices.

3. The monetary targets need of course to be supported by a consistent policy for public borrowing. The 1983 MTFS suggested a PSBR for 1984-85 of 2½ per cent of GDP, or £8 billion. As you know, I believe it would be right, for three reasons, to aim a little below this:-

(a) First, interest rates are still high both in nominal and in real terms. Lower public borrowing will ease the domestic sources of pressure on our interest rates, and insulate us to some extent against possible disturbances arising from uncertainties about the outcome of United States policies.





(b) Secondly, special sales of assets may bring in some £2 billion next year, or nearly £½ billion more than was assumed at the time of the 1983 Budget. The monetary benefit from this form of reducing expenditure is smaller than from other forms, and we must allow for this in settling the size of the PSBR.

(c) Thirdly, 1984-85 may be the peak year for North Sea revenue, and therefore ought to be a year in which to make a substantial reduction in borrowing; thereafter the PSBR would need to decline only very gradually.

I have of course taken full account of the views expressed in Cabinet on 9 February, and I shall not take a final decision until the latest revisions to the forecasts are available. But my present intention is to publish a figure of 2½ per cent of GDP, or some £7-7½ billion. The reduction on the 1983 Red Book figure would demonstrate that we had taken account of the three factors mentioned above. Publishing £7-7½ billion would put borrowing firmly back on track after the likely PSBR overshoot this year. And the latest forecast suggests that it would be consistent with the neutral Budget I envisage, and would still leave us a safety margin in hand, which we both think important.

4. The MTFs would show an illustrative path for the PSBR declining further to 1½ per cent of GDP in 1988-89, with room for cutting taxation next year and over the remainder of the life of this Parliament - provided of course that firm control on public spending is retained. The path shown in the MTFs will of course be consistent with the assumptions to be used in the Green Paper on expenditure and revenue in the longer term.

If any of the numbers mentioned above cause you any concern, I should of course be happy to discuss them.

A handwritten signature in dark ink, appearing to be 'M.L.' or similar.

N.L.

20 February 1984





cc

CST  
 FST  
 MST  
 EST  
 Sir P Middleton  
 Sir T Burns  
 Mr Battishill  
 Mr Cassell  
 Mr Lankester

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

PRIME MINISTER

In our Budget discussion on 22 February I undertook to let you know my eventual proposal on the 1984-85 PSBR.

2. At that time I had in mind publishing a figure in the range £7-7½ billion, consistent with a revenue-neutral Budget. I have now concluded that it would be possible to publish a figure towards the bottom of that range, probably £7.2 billion, (which will be rounded down, in the summary tables in the Red Book, to £7 billion), while keeping a margin in hand, as we both think sensible.

3. £7.2 billion will be £1 billion below the target for this year, and a more substantial reduction of this year's expected outturn, which we are still putting at around £10 billion. As a proportion of GDP the PSBR would fall from 3½ per cent to 2½ per cent. This should have favourable market consequences.

4. For the years further ahead I still plan to chart a more gently declining path, with the PSBR ratio falling to about 1½ per cent by 1988-89. This would, on the expenditure totals and GDP growth rate of 2½ per cent assumed, imply substantial room for tax cuts in subsequent budgets.

5. I should mention one further change to the presentation of the MTFs. Our initial plan, as you know, was to include M2 and PSL2 as monetary targets, subsidiary to the main targets, M0 and £M3. However, M2 has recently been affected by some substantial data revisions because of changes in the terms of building society deposits. This makes its future behaviour more uncertain, and I have concluded that it would be best to confine the target ranges to M0 and £M3. M2 and PSL2 will still be mentioned in the text, as aggregates to which we shall pay particular attention in interpreting the performance of the targetted aggregates, but their significance will clearly be lower than if they were target





aggregates. I myself preferred from the outset the idea of only 2 target aggregates - one broad and one narrow: I was prepared to settle for the previous formulation because it seemed likely to ensure the co-operation of the Bank. The Bank now share our increased concern about M2, and the Governor has confirmed that he is entirely content with the new formulation. I shed no tears over the change.

A handwritten signature in black ink, appearing to be "N.L." with a small flourish at the end.

N.L.

6 March 1984



~~BUDGET SECRET~~

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*Spure*  
*CCP*  
 cc PS/MST  
 Sir P Middleton  
 Mr Cassell  
 Mr Monger  
 Mr Battishill  
 Mr Griffiths  
 PS/C&E  
 Mr Wilmott (C&E)

*PSY*  
 Treasury Chambers, Parliament Street, SW1P 3AG  
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PRIME MINISTER

I am writing to let you know what I have in mind for indirect taxes in the Budget.

2. Given the severe constraints in this year's Budget, I badly need to increase what little scope I have to raise thresholds by a further rise in indirect taxation. At the same time, it is clearly important to limit the effect of any increases in indirect taxes on the RPI. Accordingly, I have in mind a package that would raise in a full year some £300m over and above indexation, but would do so without a damaging effect on prices.

3. On the motoring taxes, I propose that the extra burden should fall on Vehicle Excise Duty. Nicholas Ridley and I have agreed that the duty on cars should be raised to £100. This is more than twice revalorisation, but it provides substantial extra revenue for a comparatively low RPI effect. We have also agreed that the increase in VED on goods vehicles should average out at 1½ times revalorisation. For petrol and derv I propose increases strictly in line with indexation, giving an extra 4.1p a gallon on petrol and 3.5p on derv. This should minimise both the impact on business costs and criticism of rising petrol prices by the rural motoring lobby.

4. For drinks, I have in mind an increase of 1½p a pint on beer, 6p a bottle on table wine, and 10p a bottle on fortified wine. These increases are about 1½ times revalorisation. For spirits, I propose an increase of only 10p a bottle, well below revalorisation, to recognise the difficulties on the Scotch whisky industry, a home producer of some importance to employment in Scotland.



BUDGET SECRET



5. As to tobacco, I intend to make an increase of 6p for a packet of 20 cigarettes. This is again about  $1\frac{1}{2}$  times revalorisation but will be generally accepted on health grounds. I would propose no increase in the duty on pipe tobacco or cigars, both of which are produced mainly in areas of high unemployment.

6. These increases would yield some £250m in a full year, over and above strict revalorisation. The RPI impact will be about 0.5 per cent, of which 0.4 per cent represents revalorisation and 0.1 per cent the additional revenues. This is less than the increase of about  $\frac{1}{4}$  per cent produced by the last Budget (including the VAT changes) so that the effect of the proposals would be to produce a slight fall in the annual figure.

7. Finally, VAT. Whatever the long-term arguments for shifting more of the burden to VAT, I believe it would be wrong to make a big move in that direction this year. I therefore propose only to bring newspaper and magazine advertisements (but not newspapers and magazines themselves) into the tax. This would raise £50m in a full year, with no impact on the RPI. I am also seriously considering a small change in the VAT treatment of credit card companies which would increase revenue by up to £20 million a year.

I would be grateful to know if you would be content with these changes.

A handwritten signature in dark ink, appearing to be 'N.L.' with a flourish.

N.L.

26 February 1985