

PREM 19/145

Part 2

Confidential Filing

The 1979 Budget. Review of
Corporation Tax and Stock Relief.
Renew of Capital Taxation. The 1980
Budget

ECONOMIC POLICY

Part 1: May 1979

Part 2: June 1979

Referred to	Date	Referred to	Date	Referred to	Date	Referred to	Date
18.6.79							
19.6.79							
20.6.79							
21.6.79							
4.7.79							
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22.2.80							
23.2.80							
29.2.80							
PT 2 end							

PREM 19/175

PART 2 ends:-

TL to PM 28.2.80

PART 3 begins:-

Chan. Gx to PM 29.2.80



RM

10 DOWNING STREET

PRIME MINISTER

Sam

RM 29/2

MEETING WITH THE CHANCELLOR,
FRIDAY, 29 FEBRUARY, 1500 HRS

The Chancellor wants to outline his budget proposals. It will be two or three weeks before final decisions have to be taken, but he needs a steer from you on the broad strategy. I understand he will be giving you a note on this later tonight - if not, first thing in the morning.

You might also discuss with him the correspondence in this folder about the Local Authority spending out of asset disposals. You said you wanted to raise this with the Chancellor.

28 February 1980

TL



Confederation of British Industry

From the President:

Sir John Hedley Greenborough KBE

21 Tothill Street
London SW1H 9LP
Telephone 01-930 6711
Telex 21332
Telegrams
Cobustry London SW1

28th February 1980

Dear Miss Stephens, *Ms*

CBI 1980 Budget Representations

Sir John Greenborough sent the Prime Minister on 18th February a copy of the CBI Budget Representations.

I now have pleasure in enclosing a copy of the printed version of these Representations, which has become available today.

You may wish to substitute this for the 'rough' copy originally sent.

Yours sincerely,

Patricia Calpin

Personal Assistant to
The President

Miss Caroline Stephens,
Personal Assistant to The Prime Minister,
10, Downing Street,
London, SW 1.


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 loc Adam Ridley
 ELON

10 DOWNING STREET

22 February 1980

The Rt Hon Sir Geoffrey Howe QC MP
 Chancellor of the Exchequer
 HM Treasury
 Parliament Street
 LONDON SW1

Dear Geoffrey,

Following my letter of 20 February on the Budget, referring to getting the big numbers right, I did not mention council rents in the context of mortgages. It does seem that this is an area where, though I can see the difficulties, bold measures would make a huge difference. I realise this is rather academic now, but one could think of announcing a planned increase - or a range of increases - of rents, to bring them into line with the reality over 3 years - ie over TIME. Since they are "tighteners" not "looseners", the earlier you warn people, the better.

On the question of presentation, I was talking to David Howell today who was reiterating his concern that people didn't understand the impact of oil price rises on raw material prices and price levels generally. If, at last year's Budget, we had had the sort of presentation I suggested in my recent paper, with "what if" questions, we could then anticipate such external shocks, warning people in advance so that, if and when such shocks take place, you can then refer back to the Budget presentation without appearing to make excuses.

We are really getting back to the question we discussed on the Fentiman day - the importance of establishing the criteria, at the beginning, by which people can judge what happens in the event. The Budget presentation could be a way of doing that, of helping people to understand that we live in an uncertain world.

In the past, the convention is that Chancellors insult people's intelligence by treating them as if the world is certain, and the Chancellor is Father Christmas handing out a whole lot of goodies to the people - you know the sort of thing, "this year, I have tried to do a little more to help such and such a group". It all sounds like ad hoc acts of charity with other people's money. We must use the Budget, like everything else, to educate people by treating them as adults, remembering that our target is the electoral margin.

Yours ever

JOHN HOSKYNs

PERSONAL AND CONFIDENTIAL



10 DOWNING STREET

20 February 1980

The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer

Dear Geoffrey,

Here is the promised paper on the Budget and Budget presentation. Norman and I will be doing further thinking on the presentation side, and perhaps we can talk about that in two or three weeks' time.

Yours sincerely
A handwritten signature in dark ink, appearing to read 'John Hoskyns', with a horizontal line underneath.

JOHN HOSKYNS

BUDGETINTRODUCTION

- 1.1 This note contains our thoughts for the 1980 Budget, setting it in the expected political context of the Employment Bill and the steel strike, and the general question of economic expectations. Not being an economist, of course many of the suggestions may not be workable, either for logistical reasons or because there would be secondary and tertiary effects of which I am unaware.
- 1.2 As you know, I felt last June that the whole situation was far too serious for us to concentrate on MISC 14. I felt we should have focussed on a major and explicit "Stabilisation Programme" and we could then have started work on the indexation problem. With hindsight - always easy - the June Budget could have been more of a shock package, and presented as such. But that was one of the inevitable problems in the heat of taking office, particularly as we had a Budget on the critical path from day one.
- 1.3 Because we've never had any of the Chequers teach-ins on Government Strategy of which there was talk just after the election - and which we are now thinking about more positively - I suspect that many of the colleagues still have no concept of the make-or-break nature of our economic strategy and the fact that there appears to be no smoother ride available.
- 1.4 We must assume that our opponents, from the Right of the PLP to the far Left of the union movement, are having some success in representing us as a divisive and class-based Government - not the ideal setting in which to introduce a very tough Budget - so we will have to work hard at the communications and possible symbolic policies. These symbolic policies and soft words are necessary as much as anything in order to soothe the nerves of those colleagues and back-benchers who don't understand how near the edge of the precipice we are, or who won't face up to it.

2. BUDGET OBJECTIVES

- 2.1 There are two distinct objectives. First, obviously the Budget arithmetic has to be right so that the balance is what you, as Chancellor, want. Second - related but different - the shape of Government spending has to be altered in such a way that it is stable, so that it doesn't simply grow in uncontrollable and increasingly distorted ways. As we know, automatic indexing makes the economy hard to control, in terms of both total public spending and the distribution of that spending.
- 2.2 We have so little time, and so much ground to cover, that I feel one has to start by saying: "If there were no political and social constraints, what would we want the main numbers to look like, for the economy to regain flying speed?" Then we have to see how we can so shape the package, in the sense of "a fair deal in an emergency", that people will accept it with a sense of unity, rather than simply blame the Government for disappointing their

expectations. Are there symbolic policies which would prove that we are not taking these tough measures because we are fighting a class war, but precisely because we are determined to get the answers right for everyone's benefit - "cruel to be kind"?

2.3 There are really three parts of the public expenditure exercise:

- The big numbers (housing, transfer payments of all kinds) which we have to change fast, before the whole system goes under.
- The expenditure follies - locust institutes or whatever they were - which take time to hunt down and scrap.
- Improving cost effectiveness - the Rayner exercise - which again is a voracious consumer of quality manpower and takes time.

I fear we are slipping into the wrong mode and, instead of going for the big numbers and being brave, we are going for the small numbers and looking mean.

2.4 You remember at our working dinner with the Prime Minister and Keith January I used the words "shock package". It was disappointing that the Indexation Group stopped looking at the lessons of Belgium, "Loi Unique", as soon as it read about the riots! No questions were asked about whether the riots were avoidable, whether there was anything to learn from the economic measures then taken, in their effect on Belgium's economic recovery. We have our riots - and deaths too - at Hadfield, Red Lion Square, Grunwick, Southall - but without any economic benefits. It's not a question of foolhardy confrontation etc, but of looking calmly at others' experience in similar situations of emergency, and asking what is to be learned.

In many ways, I feel that the more severe the "shock package", the easier, not the harder, it will be to sell. I'll come back to this point in section 4 below. The problem we have to face is that most people have given up expecting any Budget to work, any Government to solve the problems - and they don't really think the problems are their fault (which, to the extent of OPEC, of course they're not). I had hoped that we would be able to weave three things together: the steel strike, the Employment Bill, and the Budget, in order to focus public impatience on the futility of union action and then combine a tough Budget for everybody, with a toughened Employment Bill for the unions. The tough Budget would also have been our fallback position and the whole thing would have hung together. However, our opportunity to dominate that debate and link these three things together has probably passed.

3. A POSSIBLE APPROACH

3.1 Indexation and de-indexation

3.1.1 Although the ad hoc group has made considerable progress with this confusing subject, it has, still not, I think, reached what MIT call "the second level of insight". The connections are somehow

still missing. Getting to grips with such a subject is inevitably an iterative process, and I felt there were one or two iterations still to go. This section attempts to telescope those final iterations.

- 3.1.2 There has been some confusion about the objectives of indexing and de-indexing. Sometimes we have been talking about living with inflation, sometimes about ending it. At other times, about a different but related objective - de-indexing simply in order to cut public spending.

De-indexing obviously is necessary in order to cut spending. De-indexing tended originally to be confused with partial indexing, which was regarded with suspicion because it was seen as a form of incomes policy. Those inhibitions have gone now, though the words "partial indexing" are not used and instead the report talks of discretion to index less than fully.

Much of the discussion about indexing (as distinct from de-indexing and its usefulness in either living with or ending inflation (confusion often existing about which objective we were talking about at any one time), always turned out to refer, by implication, to full indexing. But everyone agreed that full indexing was, by its nature, destabilising - and horrendously so under the impact of external price shocks. By contrast, the context of partial indexing - which surely must be a damping device, in the control system sense - was, as I say, ignored in the early discussions.

Having gone round in circles a bit, we eventually came to three pretty clear conclusions:

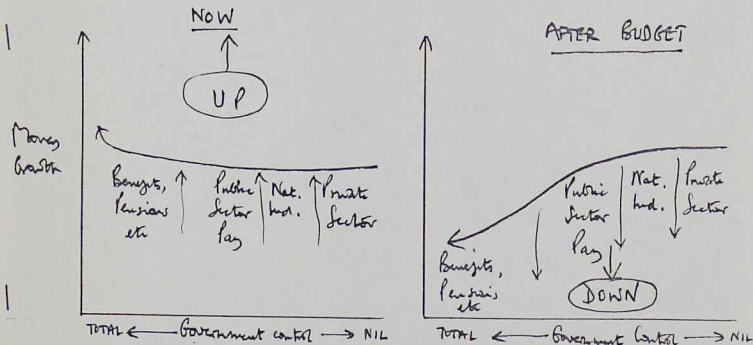
- (1) Our overall purpose is to help us to end inflation, not to live with it - though discussion still tended sometimes to proceed as if the aim was the latter rather than the former.
- (2) Fully indexed "blank cheque" commitments must be, de facto, partially indexed, by the exercise of Government discretion.
- (3) This principle of partial indexation may need to be extended, to avoid distortion and achieve fairness; and the extent to which it was partial, in percentage points, must be uniform for presentational fairness. A stable currency is, after all, effectively an indexation of everything at the same (zero) inflation rate.

- 3.1.3 How the process would work. We have a spectrum of control for indexing purposes. At one end we have those things completely under Government control like benefits and allowances and tax bands, at the other we have the private sector subject to market pressures and conceivably to exhortation. In the middle we have the public sector, where the Government can exert some influence.

Given that we cannot in the end get inflation down unless money incomes fall, if we are to avoid excessive transitional unemployment

where should the money income deceleration start? Our original policies assumed that it would have to start the hard way in the private sector, under pressure of unemployment and bankruptcies. This has always seemed to me to be the wrong way - or at least a very difficult one - because, as we have argued before, highly competitive unions, under economically illiterate union leaders, are simply forced, in general, to outdo each other's attempts to outdo anticipated inflation. That really is an unstable situation. It could never make sense for us to wait for that to turn, while the rest of the system (public sector pay under Government influence, and social security payments under Government's absolute control) remained fully indexed! So start at the other end. Everything that Government pays out must be immediately partially indexed. That is the leading edge of money income deceleration. Government must then treat as top priority making public sector pay follow suit, no doubt with a less sharp deceleration and a little later, in time. We have to get away from comparability, to something like comparability - X%. We may even have to consider a partially-indexed freeze in the public sector, but that would have to be thought through in the context of a larger package. This, coupled with trade union law reform to tilt the balance in both private and public sectors, should really be the central focus of all our efforts over the next 3 years.

That process would begin to reduce the inflationary pressures in the private sector in three interconnected ways. The first is the direct pay and benefit comparisons made by negotiators; the second is the easing of Government's blank cheque commitment to welfare beneficiaries; the third way is the more indirect consequence of the first two, through the resulting reduction in the PSBR and thus interest rates.



It will be very important that spending Ministers really understand that this process is crucial and that its aim is not the continual reduction of the real value of benefits, but the triggering of a systemic deceleration in money incomes, and thus more easily in money supply.

In "selling" these measures, internally and to the public, it must be stressed that they are part of a programme to end inflation,

not to live with it. The measures themselves must by definition be "self-obsolete" over a few years. (Does that mean that they should be dismantled thereafter, or do they have a longer-term value? I don't know.)

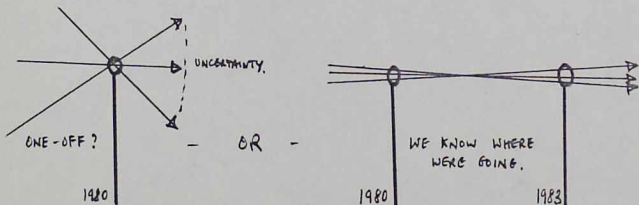
- 3.1.4 Rough justice, broad package. The package must be intelligible in space and time. The more clearly it has a time dimension with a goal and purpose, and the broader it goes, the more it will be perceived as hopeful and fair.

On the face of it, I am not sure that it is logical to only partially index rules (eg allowances and thresholds) in the same way as we partially index actual payments (eg Supplementary Benefits, public sector pay), unless we are saying that private sector pay, which is regarded by the group as automatically and fully self-indexing, should be partially indexed through the income tax system. The private sector might well remain fully-indexed, but: (a) it is subject to supply and demand; and (b) it would in any case be following benefits and public sector pay down. The group could not decide whether fiscal drag helped to cure inflation (by reducing the PSBR) or made it worse (by increasing wage pressures). But it may be that rough justice, in which everything that is going to be indexed or de-indexed is done at the same percentage of the inflation rate, is necessary because it would be too complicated to explain the reasons for doing anything different. The exception would presumably be indexed gilts.

It is a great pity that we are committed to indexing pensions in line with prices, since 5 percentage points of such big numbers would presumably make a big difference. De-indexing of public sector pensions above £1,000 a year will presumably make little difference, but it may be a useful symbolic measure.

3.2 The Time Dimension

- 3.2.1 The Budget as a whole, and the indexing measures in particular, have to alter people's expectations. They must calm people's minds as much as they stabilise the economy. A single Budget points in no direction. We need to plot some sort of framework into the future to give that sense of direction and hope.



Provided that, wherever the Budget makes long-term commitments,

they are fiscally tightening rather than promises of good things to come, there should be no difficulty. Where such pledges promise good things to come, they should only be in areas where the total numbers are small and one can therefore make the pledge with an easy mind. You remember before the election I suggested that top tax rates should come down in stages over 3 years. This would have been presented in the context of a "national emergency" Budget, extracting maximum political capital from that symbolic gesture, knowing that, because the total numbers were not large, it was one of the few promises you could safely give.*

- 3.2.2 It is in this longer timescale that the symbolic measures (eg over perks, and also over mortgage interest relief) would apply. We still seem completely confused over mortgage interest relief which has gravely distorting effects on the economy. We defend them as part of our social philosophy but at the same time tacitly reduce them by back-door de-indexing.
- 3.2.3 Valorisation of duties could be done over time so that (just as we do with phasing out of regional aid) people have time to adjust. Otherwise we'll end up with whisky being cheaper than petrol. Alcoholism is already estimated to cost the country £4bn a year (I think) according to the CPRS study.
- 3.2.4 The Rate Support Grant might be wound down in a systematic 4-year programme in the same way, so that there could not be instant uproar about arbitrary or capricious cuts. Councils would know, 3 or 4 years ahead, that RSG was coming down by X percentage points each year. It's an area where you can commit yourself, since it is a tightening rather than a loosening pledge. And they will then know where they stand, instead of having uncertainty followed by a fresh shock each year.
- 3.2.5 If there are to be major changes in capital taxes, I again suggest that they should be reduced over time, not all at once. There is so much bad news about now, and so much ammunition for our opponents to use in presenting us as stony-hearted, anti-union, anti-working class etc, that we really should be sensitive. I would advocate making any reductions gradually, and devoting great effort to explaining that, even though they are higher than in other countries (if that is the case), we are not, in today's harsh circumstances, going to bring them straight down. We should be quite explicit and say that we are phasing the reductions over time purely on symbolic grounds, grounds of fairness, because we understand how people feel. There has to be a point - and we can say so - at which we deliberately become economically illogical in order to retain contact with the great majority of people who have little capital to speak of and who will easily misjudge our actions and our motives.*
- 3.2.6 Personally, I would have liked to look again at the accessions tax idea as part of the symbolic package, because it helps to do something we have not yet done: paint the picture of the type of society we are aiming for. At present, it looks like a "rich get richer" society rather than an equal opportunity society. I

* I know that conventional political wisdom says that's not possible, "you have to do now, because you won't be able to later". But at times of discontinuity you need innovation, not convention.

believe that all our thinking about how to hold the whole social and economic system together and give it a new sense of direction, cohesion and hope, is still pigmy-thinking when set beside the UK problem. The inefficiency costs of faulty allocation etc must be balanced against the social and political costs, at a time of great stress. Perhaps we really won't wake up to it until after we've lost the next election. We have the choice of being radical or politically obsolete. However, this is probably a minority view!

4. COMMUNICATIONS

- 4.1 I believe there is a sort of "perception threshold". Below that threshold, life appears normal and this Budget is just another Budget presented with a lot of double talk and unlikely to make the faintest difference to anything. Above that threshold, it can become more drastic and yet be welcomed for it. Once it is above the threshold, and therefore looks bold (in the sense of being tough, not in the sense of being a high-risk give-away, which of course it can't be) and fair, and provided it is likely to be seen by the media (who will pass the message on) as likely to work - then one can make it bolder still! This is why I felt it was a pity we didn't look more carefully at the Loi Unique, because we don't live in normal times. Britain behaves as if it does, which is why it fails.
- 4.2 Whatever the shape of the Budget, it must be presented in a way which communicates a sense of strategy and direction to the electorate and there must be no double talk, no presentation of Rooker-Wise as tax reductions, or de-indexation as if it was "no change". The money illusion has gone. There is no chance that people (certainly at the electoral margin, and probably anywhere else for that matter) will be fooled. The messages accompanying the Budget will have to be carefully designed to make Labour and the unions' reaction look irresponsible and out of date.
- 4.3 Norman and I have done some thinking about how the broadcast might put the Budget over. Here are just a few thoughts, in no special order:
- (1) Make it fresh, interesting, different. Perhaps some "what if" questions - even a computer display. If wages do this, if OPEC does that, what are the outcomes?
 - (2) You could outline the boundaries within which you have to operate. "If we could persuade everyone to take no increases, and we completely stopped indexing all benefits, the numbers would look like this - inflation could come down very fast. But in a free society we have to accept that it won't be so simple. At the other extreme, the Government could make itself very popular by cutting this and raising that and you'd all think it was a wonderful Budget - but look at what would happen to prices, look at what would happen to unemployment, look what would happen to interest rates etc."
 - (3) Talk deliberately in a timeframe which takes you beyond the next general election.

- (4) You could be quite explicit about public sector pay, explaining how the de-indexing is designed not to make the whole burden fall on one group - that we cannot have - but to trigger the process of a decline in money pay increases. If you make it clear that we have to lean on public sector pay, with the reasons, for the benefit of stable prices for all, they can't really complain later. It is almost advanced consultation. "If you really don't want that, then don't say I didn't warn you. Now's the time to start looking for jobs elsewhere. If you can't get them, perhaps you'll realise there are advantages in being in the public sector."

- 4.4 The aim should be to talk about a range of outcomes, to remind people that we live in a small economy in a dangerous world, that oil and union behaviour could upset all our calculations (no reason why you shouldn't refer to the Green Paper, the fact that everyone knows that the eccentric British trade union law makes our Budget and economic management a more difficult problem than it is in other countries). Show people that it is a probabilistic exercise, not a book-keeping procedure. Don't worry about talking over the heads of the audience, give them something that really makes them think. The papers will tease out the message for those who don't immediately understand it. The end result should be a heightened awareness of the fact that we'd better behave sensibly together in a small island economy which is going slowly down the tubes, and should make Healey's response sound like a lot of obsolete guff.
- 4.5 Though there will obviously be secret information problems, Norman and I would be very happy to work with Tony Jay and perhaps Terry Burns (with his extensive economic model experience) to see if we couldn't put together some really interesting visual and educational modules.
- 4.6 Finally, nothing to do with communications, one further thought. The more of a shock package it is, the more you should think seriously about having a special impost upon the upper tax rates. This will horrify you even more than my original suggestion about phasing the top tax reductions. But a little bit of symbolic policy could buy you a lot of room for getting the anti-inflationary arithmetic right faster, and we haven't much time. At the moment, all our "economic realism" is linked to two things: first, incomprehension by the public, so that there is fear of the unknown, of an uncertain and frightening future; second, divisiveness which must at the margin make more and more people wonder whether we are the dreadful party the Left tries to paint us. If we can take that same realism and couple it with concrete evidence of fair-mindedness, and also, by exploring the future in terms of "what if" questions and different outcomes, so that it is a nasty future which is known rather than a much more frightening unknown, then our realism could lead to hope instead of fear.



Wed Feb 20th 87

H M Treasury

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Parliament Street London SW1P 3AG

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A N Ridley
Special Adviser

Dear Tim,

R. W. T.

I am sending you, herewith, some notes which might be of some interest to you as the budget approaches. As you will be aware, I am in regular contact with a range of outside opinion at all times. At moments such as the present their views tell me a good deal which one does not hear inside this building. That is not to prejudge, of course, who is right or wrong.

The notes are not very
hard in places, I'm sure I did
them in something
of a hurry for a
meeting.

If you think the PM would like
to see all or part of them, I can
see no reason why one should not
show them to her. But I leave
that to you.

Yours

Adam

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20 February 1980

I am writing to acknowledge your letter of 18 February with which you enclosed a copy of the CBI's Budget Representations. I have placed this before the Prime Minister.

T P LANKESTER

Sir John Greenborough, K.B.E.



Secretary of State for Industry

SECRET

DEPARTMENT OF INDUSTRY
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20 February 1980

The Rt Hon Geoffrey Howe QC MP
 Chancellor of the Exchequer
 HM Treasury
 Parliament Street
 LONDON
 SW1

Dear Geoffrey,

As you consider the balance and main constituents of the Budget, you may wish to have a note of the industrial position as I see it, and the priorities I favour.

This letter is, of course, written without benefit of the latest National Income Forecast now being formulated. I share your reservations about forecasting, especially in present conditions, and I understand that you want to keep the forecast to as minute a circle as possible at this time. Nevertheless, I hope you will agree that I may see the forecasts submitted to you, as I did last Summer though not in the Autumn. I should not be surprised if the forecast indicated a significantly higher earnings and price level increases than in the Industry Act forecast, and a substantially sharper fall in GDP and - more especially - in manufacturing output. The consequences of such trends for corporate liquidity would be very serious and I return to that below.

I understand and strongly share your concern at the likely size of the PSBR, which will be aggravated by the effects of the steel strike, by the adverse trends in earnings, prices and activity suggested above, if they materialise, and by the lower expected output from the North Sea. The effects on interest rates if a PSBR of £10-11b had to be financed would be deeply worrying. I assume from our discussions in Cabinet that the greater part, if not the whole, of the further public expenditure cuts together with sales of assets and any reduction in our EEC contribution will go to reduce the PSBR; and that there will be little if any headroom for net tax reductions - indeed quite possibly the reverse.

The corporate liquidity situation seems to me of pivotal importance. Pressure on corporate liquidity is, of course, one of the mechanisms by which our monetary policy is intended to operate on inflation expectations and wage demands. But there may come a point at which that pressure entails unacceptable damage in two areas - the chances of survival of potentially viable parts of our industrial structure (which we

SECRET

Copy for David Wolfson Mr. 2 of 12 Copies 7
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Prime Minister

Sir Keith argues for a reduction in the fiscal burden on industry because of the poor prospects for corporate liquidity - even if this means not fulfilling Bosker/wise

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cannot assume will all automatically be picked up and restored to life out of receiverships); and the maintenance of a reasonable level of investment during the recession so that industry can enter an upswing in reasonable shape, rather than becoming even more debilitated and obsolescent. Somehow we have to judge whether that point has been, or is likely to be, reached; and if so how best to adjust for it.

The inter-Departmental official group on Industrial Finance, which reviewed the prospects for the corporate sector in the light of the Industry Act forecast, envisaged a corporate sector deficit (excluding North Sea companies) in 1980/81 a little less severe than in 1974 (4% of GDP compared with 4½% then). It suggested, however, that manufacturing might be under particular pressure compared both with other sectors and with manufacturing's own position in 1974, even after making substantial reductions in stocks and investment. And it suggested that "perhaps the greatest cause for concern is that this retrenchment by companies will prolong the recession, delay the recovery and further damage output and employment growth". I fear that the forthcoming National Income Forecast will imply a still further significant deterioration in the prospect for industry in general, and for manufacturing in particular, in 1980/81, and that the financial position for the corporate sector may be substantially worse than 1974.

In these circumstances the first point I want to make on the content of the Budget is that, at the very least, there should be no question of actually increasing direct burdens on industry in the Budget. I have in mind particularly the suggestion that we should block VAT deduction on road fuel used by business, with a cost of some £525m in a full year to industry (or £275m for petrol alone); and the suggestions that monthly repayment of VAT to repayment traders should be ended. I hope you will also consider whether any increases in the specific duties can be avoided or moderated where they are of particular weight for industry - the heavy fuel oil duty is a prime candidate here, and Derv is another, for both of which there is a respectable economic case for exemption from revalorisation. But the point is of general application, and I hope you will consider carefully whether any changes you may be contemplating would have direct or incidental adverse effects for corporate liquidity, and avoid or mitigate those effects if possible.

My second point is that I hope you will look closely at the possibility of substantially increasing the take from the North Sea. I think there have been two principal reasons for caution in this area hitherto: the undertakings given to North Sea operators, and the risk of delaying exploration and exploitation. As to the first, whilst I appreciate you have already accepted



3.

the last Government's increases, and yourself accelerated payment of PRT, I feel strongly that the recent huge increases in world oil prices and producers' margins fully justify a windfall profits tax (using some instrument which would bring in the additional revenue now rather than with delayed effect as would happen by adjusting PRT rates or allowances). As to the second, if we agree that depletion should be delayed, it seems sensible that we should use tax increases as part of the mechanism to bring this about, and thus kill two birds with one stone. Of course delayed depletion will mean reduced revenues in the medium-term; but a sharp increase in the short-term offset by smaller revenue in the medium-term does fit the profile of our monetary requirements. I believe there is scope for securing very substantial additional revenue in the short-term from the North Sea without unacceptable penalties. I should strongly resist accepting serious damage in the non-oil corporate sector (especially manufacturing) which could have been mitigated by more vigorous action on North Sea taxation.

Third, on the assumption that significant additional revenue is obtainable in the short term from the North Sea, there are several broad directions in which that benefit could be deployed. It could be used to make further progress on our objective of cutting income tax, either on the allowances or on the basic rate. Or it could be used to cut back the PSBR as a proportion of GDP lowering interest rates and releasing resources for private sector use. Either of these, of course, would be welcome in normal circumstances. With some misgivings and after careful thought, however, I have myself concluded that now is the time to direct fiscal easement to the corporate sector. There are of course several possible ways of giving relief but the most satisfactory in my view would be to remove the whole of the National Insurance Surcharge. We spoke about this in November and I said then (in my personal letter of 9 November) that I agreed we could not at that stage decide to reduce the NIS, but added "company liquidity looks awful and may look even worse - and that is why I have to emphasise at this stage." I am aware that changing the surcharge mid-year entails serious administrative penalties for the DHSS and for companies, but I believe those factors have to be subordinated. Alternative reliefs, for example, on the Corporation Tax rate, would not necessarily be widely enough spread or give direct help to the right companies.

Also in the corporate sector, I would put a very high priority on adjustment to the stock relief arrangements to avoid a heavy tax charge where there is a temporary reduction in stock values, about which I have already written to you; this is likely to be a serious problem not only for firms hit by the steel dispute but more generally in depressed trading conditions.



These easements to the corporate sector would by no means remove the acute financial pressure on companies. With industry operating on average at about break-even in real terms, and faced with the necessity of making major cuts in investment programmes, product development expenditure, R & D, stocks and manning levels, I do not think it should be assumed that an easement of this size will lead to a major extent into higher wages. Given the present level of competitiveness of British industry (caused immediately by the exchange rate), any leakage is much more likely to be into prices which would be helpful for our counter-inflation policy, for exports and for manufacturing output.

I believe that the strong case for some easement to the corporate sector stands even if you are unable to secure early additional revenue from the North Sea. I accept that, given the overall conjunctural prospect, to reduce fiscal burdens on industry without additional oil revenue and without increasing the PSBR is likely to entail increases in taxation in the personal sector - though because it could not be implemented until later this year the cost of abolishing the NIS would not be overwhelming in 1980-81. I appreciate the attractions of sharp increases in the specific duties on alcohol, tobacco and hydrocarbons. Given the present threatening prospects for retail prices, however, I think we shall need to be very much on the cautious side. It follows that, without additional oil revenue, the tax reductions I advocate for industry would have to be financed by higher income tax than would otherwise be possible for instance by not fully indexing personal allowances. This would be a bitter pill to swallow, and I should not advocate it were I not so concerned about the prospect for the corporate sector in the period immediately ahead.

Fourth, I know you intend to give some prominence to small firms and enterprise, and we are in separate discussion on that. David Mitchell has, I understand, given you separately his personal suggestions for further technical measures in the small firms field.

Fifth, I have already written to you about the extended reliefs for employee shareholding schemes we agreed recently in the E Committee, which are essential in connection with the privatisation of British Aerospace. I have also given you my views on the desirability of reviving the 1972 share option scheme, which would have negligible cost.

Finally, I had hoped by now to have had details of progress on two major reviews of taxation - capital taxation and corporate



.. SECRET

5.

taxation both central to my responsibilities. To my considerable regret, neither I nor my officials have been consulted on either of these, and we have therefore been unable to contribute an industrial perspective at the formative stage. Perhaps your officials could let mine have copies of the relevant documents so that we can let you have our initial reactions.

I am copying this letter to the Prime Minister.

Yours

Kew

SECRET

20 FEB 1960





Pam Paul
2 MARSHAM STREET
LONDON SW1P 3EE

My ref:

Your ref:

19 February 1980

RM

Dear Betty

- will request if required

I wrote to you on 12 February about development land tax and taxation and historic houses. I would be grateful if, in considering your Budget statement, you could also bear in mind 2 further issues which touch on my responsibilities.

Stock Relief

I would ask you to consider again the stock relief provisions. I realise that you revised these arrangements in your Budget last year, but a reduction in the clawback period from six years to four years could be presented as a measure of particular assistance to the construction industry which is very hard hit at present, with little prospect of improvement in the short term. Such a provision would be particularly beneficial to small firms and would accord well into out industrial policies; and as some 90% of the construction industry is made up of very small firms would be well received by them.

Capital Gains Tax Relief for Resident Landlords

will request if required

In your letter of 25 September you said that the question of exempting resident landlords from Capital Gains Tax must be seen in the light of Arthur Cockfield's review of capital taxation. However, I would like to take this opportunity to raise the issue again.

As you know, the Housing Bill received its Second Reading on 15 January. One of its guiding principles is the reduction of local authority housing controls, partly through increased home ownership and rights for tenants, and partly through measures designed to revive the private rented sector. As you will appreciate, an increase in the amount of privately rented accommodation is the one way in which housing needs can be met without a parallel rise in public expenditure. Indeed proposals to stimulate the sector have usually been welcomed by the Treasury as a means of reducing the need for subsidised local authority housing. A positive approach to increasing the supply of privately rented accommodation is vital given the present round of cuts in housing expenditure.

We estimate that in 1977 there were 900,000 dwellings with 2 or more "spare" bedrooms. We are determined to encourage as many home owners as possible to let their rooms and thus combat housing shortages. Two main changes are proposed to boost resident landlord lettings and tap the substantial pool of under-used accommodation in owner-occupied homes. The first is that for new lettings a notice to quit may no longer be suspended by the rent tribunal and no possession order may be postponed for more than 3 months. Second, a landlord will be able to grant consecutive fixed-term tenancies without creating fully protected tenancies. One remaining disincentive to letting, however, is the continuing threat to resident landlords of liability for CGT on the sale of their own houses. Many people feel that the taxman has it both ways - they are not treated as businessmen when it comes to claiming capital allowances, yet the situation is reversed as soon as there is a possibility of paying capital gains tax.

The estimated cost of exemption from CGT for resident landlords is minimal at £0.5m, yet its psychological impact would be great. In addition the public expenditure costs will be reduced each time a landlord who was previously deterred from letting, houses someone who would otherwise be on the local authorities' waiting list. For example the present cost of providing a local authority home for 2 people is £8,000. On the other hand, if such a couple were to be housed by a resident landlord the net result could be a gain to the public purse of income tax on the rent received.

I would be grateful if you could let me have your initial views on the possibilities of this exemption, particularly as the matter is quite likely to be raised again during the course of the Housing Bill, following Nick Scott's reference to it on Second Reading and given the steady amount of correspondence we have received on this issue. You will appreciate that our continuing inactivity looks all the weaker given the fact that before the General Election both Nigel Lawson and Hugh Rossi expressed their support for the proposal.

I am copying this letter to colleagues on E Committee and to Sir Robert Armstrong.

Yours are



MICHAEL HESELTINE

19 FEB 1980



Confederation of British Industry



4

From the President:

Sir John Hedley Greenborough KBE

21 Tothill Street
London SW1H 9LP
Telephone 01-930 6711
Telex 21332
Telegrams
Cobustry London SW1

18th February 1980

Dear Prime Minister,

Prime Minister
To glance. Summary is
at Flax A. (I have
not - automated)

I have pleasure in enclosing a personal copy of
our Budget Representations, which we discussed with the
Chancellor today.

12
209

Sincerely,

John Greenborough

The Rt. Hon. Margaret Thatcher, MP,
Prime Minister,
Downing Street,
London, SW 1.



20 FEB 1980

The Budget 1980

**CBI representations
to the
Chancellor of the Exchequer**

Foreword

This publication sets out the CBI's Representations to the Chancellor of the Exchequer for the Budget on 26 March 1980. The main recommendations are summarised on page 35.

These Representations are presented to the Chancellor after extensive consultations with CBI members, primarily through the CBI Council, Regional Councils, and Standing Committees.

The Technical Representations in Part II were submitted to the Inland Revenue last Autumn.

CBI
7 February 1980.

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Part I

General representations

SECTION 1

INTRODUCTION

The strategic objectives for government policy which will allow British trade and industry to succeed in the long-term, which we have consistently advocated,* have largely been adopted by the new government. Priority for combatting inflation, more realistic government expenditure programmes, less intervention by government in business decisions, more realistic personal tax rates, and moves toward a more even balance of advantage between employers and organised labour will all contribute greatly to future prosperity. Already important first steps have been taken - as we urged - towards these objectives. CBI support in pursuing them will be resolute.

There are however some respects in which the Government's policies have differed in emphasis from our recommendations. Short-term monetary policy has been more restrictive than we suggested, in particular because the money supply limits will operate against a background of higher increases in prices as a result of the decision to raise VAT to 15%. The VAT increase was greater than we recommended.

Nonetheless, the determination of management to accept the challenge and to drive for improved performance is strong, as was underlined at the CBI National Conference in Birmingham last November. This is the way in which the opportunities presented by the Government's sound long-term strategies can be grasped.

Such determination is essential in view of the short-term prospects for many sectors of business. On any Government policies, these would have been difficult, as a result of high inflation, weak demand and poor international competitiveness. Levels of profits, production and employment are thus likely to be depressed.

The main objectives underlying the next Budget are clear. They should be:

1. to seek major reductions in inflation as early as possible
2. to continue to improve personal incentives and free more people on low incomes from paying income tax
3. to assist companies' financial position, and
4. to reduce capital taxes and take other steps to encourage the development of smaller businesses.

In deciding on our recommendations we first assessed the economic and business prospects. The main features are outlined in the following section.

* For example, in 'Britain Means Business' 1977 and 1978, and in our Economic Policy and Budget Representations to the incoming Government in May 1979.

SECTION 2

ECONOMIC BACKGROUND

In this section* we look at the economic situation and prospects, on unchanged policies**, that form the background to our Representations.

The past year has seen large rises in oil prices, a sharp rise in the Sterling exchange rate and increased rates of inflation. Partly because of the delayed effects of these factors, in the short-term the trading climate for British business will be difficult. This is likely to lead to falling output and employment. In addition it will probably cause profit margins to be reduced still further which would cause serious financial difficulties for many companies.

Inflationary pay pressures are still widespread. Also interest rates are currently at very high levels although (as explained below) we expect a fall over the coming year.

Medium term prospects depend very much on the success of present policies aimed at increasing incentives, reducing inflation, moderating pay increases and improving productivity. If the policies are successful, and given reasonably favourable world economic conditions, we could see a sustainable recovery in our trading performance, and a return to economic growth at a reasonable rate. If the policies are not successful, stagnation or declining output could continue for the foreseeable future with price inflation remaining well in double figures.

The major aspects of the economic background are looked at in greater detail below.

UK OUTPUT AND EMPLOYMENT

Last year demand and output in the UK fluctuated considerably, largely as a result of industrial disputes and of a surge in consumers' expenditure in the middle of the year in anticipation of rises in indirect taxes. Output was 1 to 1½% higher in 1979 than in 1978. Chart 1 measures capacity utilisation in manufacturing industry.

Over the period from the second half of 1979 to the first half of 1981 we expect that GDP on unchanged policies will fall at an annual rate of 2%. This is due to four main factors. These are depressed overseas markets, sharply reduced competitiveness of much of British trade and industry, companies' expenditure restricted both because of severe financial problems and because of cyclical factors, and household spending constrained by stagnant real incomes. The decline in production is likely to be reflected in further rises in unemployment.

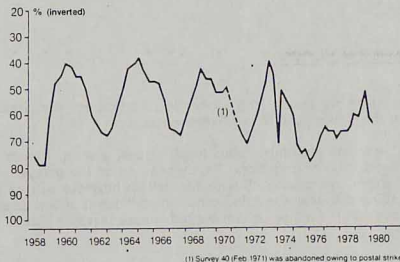
* A fuller description of the CBI view of the economic situation and prospects is given in the monthly CBI Economic Situation Reports. Figures in the text are official statistics where these are available, otherwise CBI staff estimates or forecasts.

** "Unchanged policies" are taken to mean no tax changes other than 'Rooker-Wise' indexation of personal income tax allowances, present Government expenditure plans as in Cmnd 7746, Sterling M3 growing at an annual rate of 7-11% and no significant official intervention in the foreign exchange market.

CHART 1

CBI Industrial Trends Survey

Q4 — Is your present level of output below capacity (ie, are you working below a satisfactory full rate of operation)



EXPORT MARKETS

Forecasts of the world economy are, of course, subject to a wide margin of error, particularly as a result of the uncertainty surrounding oil prices. Overall we expect little growth in the industrialised countries during the next 18 months, with a probable decline in output in the US and continuing growth in Western Europe and Japan, but at slower rates than in the last year. This reflects an expected decline in stock-building as well as the effects of rising oil prices on real incomes. In addition it seems likely that Governments will follow cautious demand management policies in the face of inflation and balance of payments difficulties.

Some of the effects on UK export markets of the projected weakness of demand in the industrialised economies are likely to be offset by higher demand from oil-producing countries. However, many non-oil producing developing countries will suffer from both the world recession reducing demand for their exports and from the increases in the cost of their energy imports. In aggregate our export markets in these countries are unlikely to expand significantly in the short-term. Our forecast for world trade growth* over the next 18 months, weighted by UK export markets, is for a small increase, at an annual rate of about 2%.

COMPETITIVENESS

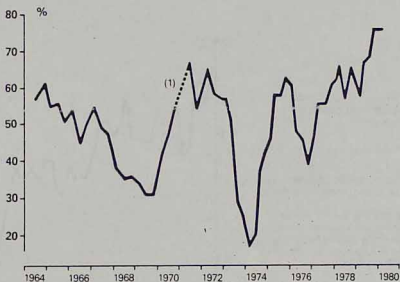
Over three-quarters of UK manufacturers in our October and January Industrial Trends Surveys, the highest proportions ever recorded, cited price competitiveness as a major constraint on new export orders (see Chart 2). This reflects the large rise in our unit labour costs in manufacturing which since the fourth quarter of 1976 have risen by over

* OECD exports of manufactures.

CHART 2

CBI Industrial Trends Survey

Q15 — Is the price of your exports (compared with those of overseas competitors) a factor likely to limit your ability to obtain export orders over the next four months.



(1) Survey 40 (Feb 1971) was abandoned owing to postal strike

60% relative to our main overseas competitors. Rather less than half of this decline in competitiveness reflects the rise in the effective exchange rate of sterling, over a third represents pay in the UK rising by more than the OECD average, and the remainder reflects mainly slow growth in our productivity relative to our main overseas competitors, and the imposition of the National Insurance Surcharge.

As a result of the reduced price competitiveness there will be considerable difficulties in maintaining our share of world trade.

COMPANY FINANCES AND INVESTMENT

Real profitability* fell from 4 $\frac{1}{2}$ % in 1978 to 3-3 $\frac{1}{2}$ % last year (see Chart 3). We forecast a further decline to about 2% in 1980, leading both to increased borrowing and to cuts in companies' expenditure on fixed investment and stocks.

The lower fixed investment, which, for manufacturing, is in line with the intentions reported in our recent Industrial Trends Surveys, will follow the rapid growth that has already taken place (private non-North Sea non-housing investment rose by about a quarter between 1976 and 1979) over a period when output has risen only slowly. The destocking reflects high stock levels at the end of 1979 in relation to output (23% of the respondents to our December 1979 Monthly Trends Enquiry, the highest ever proportion, assessed their stock levels for finished goods as "more than adequate") as well as financial factors. However the pattern of stock and production movements during 1980 will be affected by the results of the steel dispute.

* Gross trading profits plus rent less stock appreciation less capital consumption at current replacement cost as a percentage of net fixed capital stock at current replacement cost plus book value of stocks. Figures in the text exclude North Sea activities.

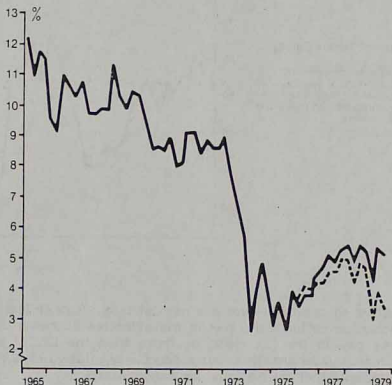
CHART 3

**Industrial and Commercial
Companies' real pre-tax
rate of return***

Seasonally adjusted quarterly data

 — Including North Sea activities
 - - - Excluding North Sea activities

* Gross trading profits plus rent less stock appreciation less capital consumption at current replacement cost as a percentage of net fixed capital stock at current replacement cost plus book value of stocks.



The financial deficit of the company sector (excluding North Sea activities) may worsen further during the first half of 1980. We are forecasting that the financial deficit may stop rising later on this year as companies cut back on stocks and fixed investment. However, this still implies a continuing high net borrowing requirement which, as the table shows, rose sharply last year. We also expect a continuing worsening in company liquidity.

TABLE 1

FINANCIAL POSITION OF INDUSTRIAL AND COMMERCIAL COMPANIES

All figures at current prices (£ million)

	Net Borrowing ¹ Requirement	Net Liquidity ² (end of period)	Notes:
1974	6,104	-9253	1 Net borrowing requirement (seasonally adjusted) measures the amount by which industrial and commercial companies' expenditure on fixed assets, stocks, trade investment, acquisition of subsidiaries in the UK, investment abroad and net trade credit extended exceeds their internally-generated funds.
1975	1,033	-7150 ³	2 Net liquidity (not seasonally adjusted) equals gross liquidity less bank advances. Gross liquidity equals end-of-period holdings of identified financial assets which include deposits with the banking sector, building societies and other financial institutions, Treasury bills, tax instruments, British government securities and local authority debt.
1976	2,845	-8663	3 Revision due principally to exclusion of companies now classified as financial companies. This 'improved' net liquidity by £1,318 million.
1977	1,585	-8095	4 New returns, starting in the second quarter of 1979, show deposits with building societies in that quarter to be £117 million less than reported on the previous basis. The effect of this was to "worsen" net liquidity in the second quarter from £8,458 million to £8,571 million.
1978	2,459	-8686 ⁴	5 CBI estimate.
1979	7,000 ⁵	-11250 ⁵	

Sources: Financial Statistics December 1979,
CSO Press Release

PERSONAL INCOMES AND EXPENDITURE

Largely as a result of cuts in taxes and, for much of the period, pay rises in excess of price rises, real post-tax incomes have risen over twice as fast as output during the last three years. Although some of the rise in incomes has been reflected in a higher savings ratio, consumers' expenditure has also risen much faster than output over this period. In the coming year our forecasts suggest declining employment. In addition, the lagged results of increases in unit labour costs during the previous two years are likely to feed into prices at a time when increases in average earnings are constrained by companies' weak financial positions. On unchanged policies, therefore, some fall in real personal disposable incomes over the next 18 months is probable. We expect the savings ratio to remain close to the average level of 1979, with consumers' expenditure showing little change.

INFLATION

Our latest analysis of recent pay settlements suggests wide variations with an average level, in the private sector, broadly similar to last year. In the coming year, as the distortions caused by years of pay control are alleviated, with a deterioration in companies' financial positions and with the demand for labour falling some decline in pay inflation is assumed although the high rates of RPI increase that may be observed up till the summer of 1980 could act as an upward influence on pay settlements.

Besides pay, two other major influences on prices in the next 18 months will be the large increases in oil prices that have recently been announced, which are likely to feed into retail prices in the early part of the year, and the rises in various Government charges and prices of products of nationalised industries which have already been planned for the next six months. In the latter part of 1980, however, the effect of these influences on the increase in the RPI compared with a year earlier will be more than offset (on unchanged policies) when the impact of the increases in indirect taxes in the 1979 Budget drops out of the twelve-monthly comparison.

We forecast, therefore, that with sterling likely to remain relatively strong as a result of firm monetary policies and North Sea oil and with commodity prices likely to weaken because of the world recession, UK price inflation will reach a peak during the first half of 1980, but could fall significantly through the following 12 months to mid-1981. However, if pay settlements continue at high levels, the decline in price inflation may be much less marked.

PUBLIC SECTOR BORROWING

We expect that the Public Sector Borrowing Requirement (PSBR) for 1979/80 will turn out at about £9 billion, slightly above the Budget target of £8½ billion. For 1980/81 our forecasts suggest that on unchanged policies the PSBR will remain roughly unchanged as a proportion of GDP, rising to about £10 billion. This is close to the centre of the range of outside forecasts. *

* Adjusted where necessary to our definition of "unchanged policies" - see footnote to page 7.

The full year effect of the rise in VAT announced in the June 1979 Budget, fiscal drag and the rise in tax and royalty receipts from North Sea activities, all of which would tend to reduce the 1980/81 PSBR relative to the previous year, are likely to be offset by the factors working in the opposite direction. These are, notably, the impact of the 'Rooker-Wise' increase in income tax allowances, the cost of public sector pay increasing faster than in the private sector, the full year effect of the income tax cuts announced in the 1979 Budget, and the effect of the declining output on tax receipts at a time when public expenditure volumes are not falling.

Of course, any forecast of the PSBR is subject to a large margin of error; errors of only 1% in the forecasts for Government revenue and expenditure, if they occurred in opposite directions, would lead to an error of £1½ to 2 billion in the forecast for the PSBR.

INTEREST RATES

In the next 18 months interest rates are likely to decline overseas and bank lending to the personal sector in the UK will be less buoyant than in much of 1979. In addition, we forecast rising inflows into the financial institutions and high demand for Government stock. On the other hand a difficult company sector financial position is likely to imply a continued increase in demand for funds from that source. On balance we expect that interest rates will fall during 1980/81. Most other forecasters agree with the view that interest rates will fall - if anything, the consensus forecast is for a faster fall than we expect.

SECTION 3

REDUCING INFLATION

There are many contributory reasons for the disappointing performance of the British economy over recent years and for the relatively poor short-term prospects. These include: poor productivity; sluggish world trade, partly because of high oil prices; rapidly rising import penetration; the effect of North Sea oil in making the pound uncomfortably high; and low profitability.

But the most fundamental reason is probably that inflation is running at well over 15%; and has been on average at this rate over the past six years - during which the value of our money has been reduced by three-fifths.

By contrast, during the first twenty years or so after the war our average rate of inflation was $3\frac{1}{2}\%$; and this was a period of unparalleled growth and prosperity by British historical standards.

If we could once again get inflation down to below 5%, many of our other problems would fall into place:

- We would be much less worried about worsening international competitiveness.
- If we were still worried about North Sea oil forcing the pound too high, we would be less inhibited about a moderate depreciation if this meant only increasing price inflation from, say, $3\frac{1}{2}\%$ to 5% than we are when it is running - as now - at 17%.
- The Government would feel freer to expand demand by cutting taxes faster (and would thus also be able to improve incentives more quickly).
- Because of higher demand at home and abroad, and lower cost inflation, profitability would be higher so that investment would grow and companies would have more to spend on marketing, developing new products, and other ways of improving non-price competitiveness.
- It would be easier in this climate of growth, with improving living standards and job prospects, to get agreement to end overmanning and restrictive practices.

This is why the CBI believes that we must get inflation down as a first priority, if we are going to get growth going again at a reasonable rate. Our German and Japanese competitors for example currently have inflation rates between a quarter and a third of our own.

The Government is relying mainly on firm fiscal and monetary policies. We fully support such policies; and this support has greatly influenced these Representations. We recognise, however, that such a strategy will work only after a rather uncertain time lag, and at the expense of some temporary loss of output and employment.

We therefore attach importance to supplementing monetary and fiscal policies by other attempts to prevent increases in unit costs, through improved productivity and realistic pay settlements, in order to minimise the temporary loss of output and jobs and the lag before a reasonable rate of growth can be resumed.

In particular the CBI has called for changes in Britain's pay determination system to secure:

- a. Better bargaining structures - for example rational structures at company and industry levels, a compressed pay round, and an end to leap-frogging between the public and private sectors.
- b. Better understanding of the economic context in which bargaining takes place - through, for example, a national economic forum and improved in-company communications.
- c. Better balance of power between employers and employees through, for example, changes in employment law, and better liaison and mutual support between companies.

These proposals are described more fully elsewhere *, and the CBI has embarked on a number of initiatives to promote them - including the production of business briefs to encourage greater understanding of economic realities, and through examination of ways to encourage greater employer unity.

No less important, a move towards greater involvement by employees in the objectives of the companies for which they work will, we suggest, promote greater understanding within industry and thus improve the climate in which negotiations are conducted.

In view of the urgency of securing much lower pay settlements, we urge elsewhere in these Representations that increases in indirect taxes should be avoided this year so far as possible and that caution should be exercised in increasing charges for government-provided services.

* For example, "Pay the Choice Ahead", February 1979 - "A New Deal for Industrial Relations", Background paper for CBI National Conference, November 1979.

SECTION 4

GOVERNMENT EXPENDITURE

Early in the course of considering our Budget Representations it became quite clear that an important element would be the achievement of substantial economies in the level of government spending. We recommend that economies of around £2 billion* should be made in spending planned for 1980/81. Economies of this scale should be achievable without damage to the economy and are entirely consistent with CBI recommendations since 1977.

In order to avoid disruption, alterations to government spending plans should be effected as far in advance as possible. Accordingly, the CBI sent a memorandum to the Chancellor on January 11** setting out its views on government spending in 1980/81. In this memorandum it was suggested that sufficient economies should be achievable by combinations of reductions in waste and inefficiency, reductions in the UK net contribution to the EEC budget, possible economies in certain benefits, stricter application of cash limits, more sparing usage of the contingency reserve and further asset sales. The economies should be made with emphasis on current as opposed to capital expenditure, and concentrated on the internal operations of government as opposed to its purchases from the market sector.

Details of the main issues and recommendations in the Memorandum regarding how economies should be achieved are restated below.

CASH LIMITS

The new system of cash limits has contributed to the increased effectiveness of control over government expenditure in the last two to three years. It is essential that this improvement is sustained. Accordingly cash limits must again be strictly enforced, and not relaxed to reimburse government authorities for any exceptional inflation of their pay or other costs. The nationalised industries themselves accept the parallel system of external financing limits, provided they are related to proper medium term financial targets.

WASTE AND INEFFICIENCY

The search for reductions in government expenditure in the past often resulted in excessive cuts or delays to capital expenditure or other procurement which have caused severe disruption to suppliers outside the government sector of the economy. This must be avoided in future and the necessary economies found in the internal operation of the government sector itself, particularly through improved efficiency.

* Equivalent to about £1½-2 billion at 1979 survey prices.

** Government Expenditure in 1980/81 - CBI Memorandum to the Chancellor of the Exchequer.

The CBI welcomes the progress that the Government has made in seeking improvements in this area but there still appears to be considerable scope for further savings. With regard to local government, the report on the value-for-money study* of Cheshire County Council commissioned last year by CBI members in that county indicated a number of areas where economies could be achieved, at least in the medium term. This suggests that, where there is goodwill and determination on the part of the local authority, there is scope for cuts in local authority spending without a serious reduction in the levels and standards of services.

We therefore support the independent application of value-for-money studies throughout local government as recommended by the Layfield Committee. We also hope to see improved government control over local authority aggregate expenditure and improved public awareness of the standard of performance of individual local authorities. These measures should have a significant effect but mainly in the medium term. There is however considerable scope for early economies in local authority manpower. In the past two years (to September 1979) local authority employment has actually increased by about 22,500** in England and Wales alone. With the number employed by local government now over 2 million** substantial savings could be achieved by way of natural wastage.

Considerable scope for economies also appears to exist in central government. The CBI supports the continued and increased use of the type of study instituted by Sir Derek Rayner, as a means of improving efficiency in the medium and long term. We also welcome the recent review of Civil Service manpower as a means of achieving more immediate economies. However the cuts so far announced do not go far enough. With the current Civil Service establishment at about three-quarters of a million the reduction of 60,000 over about three years which has been promised only implies savings of about 2½% per annum and the implied increase in productivity will presumably be considerably less as some services are to be cut and some functions transferred to the private sector. This is much less than is needed. With natural wastage running at about 40,000 per annum in the Civil Service there is considerable scope for further economies by way of manpower reductions matched by increased productivity.

In making these suggestions the CBI is by no means implying that the government sector is the only part of the economy where productivity should be increased. Clearly waste and inefficiency occur in the market sector but here at least it is subject to commercial pressures. As such pressures do not generally apply in the government sector some alternative arrangements for encouraging efficiency must be found. Moreover, the benefits from improved efficiency would be very large. For instance, a 2% manpower saving throughout central and local government would yield over £600 million.

UK'S NET CONTRIBUTION TO THE EEC BUDGET

The CBI has consistently and very strongly supported UK membership of the European Communities and has also fully supported the wider objective of promoting economic convergence and integration among the member states. However it is evident that the financial arrangements within the EEC as reflected in the various members'

* 'Value For Money: Report on Cheshire County Council' CBI September 1979

** Full time equivalent excluding police, traffic wardens, certain legal services, those employed under the Job Creation Programme and under the Special Temporary Employment Programme.

net contributions are not operating in a way which will promote economic convergence, and this is particularly obvious in the case of the UK. It is therefore as a committed supporter of the EEC that the CBI fully backs the Government in its attempts to redress the imbalance in the financial arrangements within the Community, and reduce the net contribution of the UK to the EEC Budget. The reduction in the UK's net contribution to the EEC Budget should result in an equivalent reduction in government expenditure.

SOCIAL SECURITY

Although the CBI strongly supports government's role in the care of the needy members of society, it is important that the level of social security benefits reflects what the country can afford and not just what it would like. High social security spending can only be maintained by a prosperous and productive economy. Furthermore, the social security systems should be designed to minimise any reduction in the incentive to work. The current arrangements are not satisfactory from this point of view. In the present situation where some workers may have to endure reductions in living standards the rules regarding the tax treatment and automatic indexation of benefits are likely to lead to a significant reduction in the incentive to work. The issues involved are complex, and are under study by the CBI.

A full solution of these problems cannot be achieved without the taxation of short-term benefits but this may not be feasible for some time yet. In these circumstances we recommend that the Government examine as a matter of the highest urgency the automatic indexation of unemployment and other benefits, so that when the benefit rates are revised with effect from November 1980, their rate of increase does not create inflationary pressures.

There may also be savings to be made by amending the rules governing payment of unemployment benefit to ensure that the system is not misused.

CONTINGENCY RESERVE

We welcome the reduction in the size of the contingency reserve from about 2% of total government expenditure in the previous Government's plans (Cmd 7439) to about 1% in the November White Paper. This lower figure should be more than sufficient to cover unforeseen contingencies.

The CBI fully accepts the advantages of having a realistic contingency reserve which is not exceeded rather than one which is unrealistically low and in consequence disregarded. However the contingency reserve should only be used to finance genuine contingencies. It should be clearly perceived to be a reserve covering the risk of abnormal events and therefore a reserve which is normally not fully spent. If the reserve is used in this way and particularly if early commitments are avoided, significant economies can normally be expected in this area.

SALE OF ASSETS

We welcome the Government's plan to add another £500 million (at 1979 survey prices) of (unspecified) asset sales for 1980/81 to the £1 billion already under way for 1979/80. It is important that the Government concentrates its efforts on identifying assets which are being under utilised or which because of the different pressures and obligations of the market would be better employed in the market sector - which covers both public and private sector businesses. With this approach we feel sure that the Government should be able to raise substantially more than the £500 million already planned without damaging private or public sector businesses.

PUBLIC SECTOR CHARGES

We have consistently and strongly supported the general case for nationalised industries and public bodies charging for goods and services on a commercial basis and we agree with the approach of setting medium-term financial targets for the nationalised industries within the context of their strategic industrial plans.

It would not be consistent with this approach for the Government to require the nationalised industries to override these commercial criteria, purely in the interests of a short-term contribution to reducing government expenditure. We would also urge caution in increasing charges for government-provided services which would add to inflationary pressures.

CAPITAL OR CURRENT SPENDING

The CBI has criticised past exercises cutting government spending for concentrating too heavily on the side of investment. There should be no further cuts in what the Government is planning to spend on investment in the essential industrial infrastructure.

This recommendation should not however be interpreted as meaning that all central or local government investment projects should go ahead as planned. The judgment of what is spending that should be cut cannot be simply divided under the headings of capital and current spending; but we remain firmly of the opinion that it is very much in the area of current spending that the necessary economies should be achieved.

SECTION 5

MONETARY AND EXCHANGE RATE POLICY

A central feature of the Government's counter-inflation policy has been the setting of upper and lower limits for the expansion of the money supply. Although the current limits are more restrictive than the CBI has recommended *, we support them and would support extending the period covered by a further half year to the end of 1980/81.

However, with company profitability at a record low level, and still falling, the current high level of interest rates is adding to the already considerable financial difficulties of many companies. We therefore urge that interest rates be allowed to fall as soon as is consistent with the money supply limits.

In the meantime, it is important to minimise as far as possible the burden on trade and industry of high interest rates and tight credit. This will maximise the extent to which businesses can live through the short term economic difficulties without excessive loss of investment, without company closures, bankruptcies and other reductions in the industrial and commercial base which will be required when activity recovers. We therefore welcome the continuation in force of the Bank of England's guidance to banks and finance houses to give priority in their lending to providing finance for UK trade and industry **.

We hope the current high level of interest rates will not have to continue for long. As mentioned in our assessment of economic prospects we expect, in common with most other forecasters, that interest rates will fall during 1980/81. However, the timing and the size of that fall will depend not only on the degree of success in defeating inflation but also on government expenditure, taxation and the Public Sector Borrowing Requirement.

Given the commitment to achieving a growth in the money supply within prescribed limits there would appear to be little room for manoeuvre in pursuing an independent exchange rate objective. Nonetheless the behaviour of the exchange rate is a very important consideration given its relevance for inflation and growth prospects. A high exchange rate will reduce import costs (compared with what they would otherwise have been) and may eventually help to moderate pay claims and settlements - through the favourable effects on the cost of living, and by increasing the resistance of employers experiencing pressure on their profit margins from foreign competition at home and abroad. Such competition may also increase efforts to raise efficiency, which further reduce unit costs.

On the other hand, to the extent that a high exchange rate is not offset by such factors, it will cause jobs and profits to be lost in exporting industries and those competing with imports, and prove a constraint on growth.

In view of our large loss of cost competitiveness described above, and the effects of North Sea oil on the level of sterling, three conclusions emerge clearly. First, there is a need to press ahead with measures to moderate pay settlements and raise productivity. Secondly, the National Insurance Surcharge - which is a tax on exports and in effect a subsidy on imports - should at the very least be drastically reduced at the earliest opportunity. Thirdly, a further reason why interest rates should be reduced as soon as possible is to avoid or reduce unwanted capital inflows and upward pressures on sterling.

* As explained in the Introduction.

** Notice to banks and finance houses, issued by the Bank of England on 15 November 1979.

SECTION 6

PUBLIC SECTOR BORROWING REQUIREMENT (PSBR) AND THE BUDGET JUDGMENT

Although any forecast of the PSBR is subject to a wide margin of error, a key feature of the Budget will be the central estimate of the borrowing requirement implied for 1980/81.

A figure similar to the PSBR for 1979/80 in nominal, monetary, terms would be a good deal more restrictive in real terms, ie when allowance is made for the effects of inflation and of the expected recession (which will increase the PSBR both by reducing the incomes and expenditures which are subject to tax, and by increasing social security benefits). To allow for these factors, and produce a similar fiscal stance to that in the current financial year, would imply a PSBR in monetary terms some £2-3 billion higher. For example, the London Business School has estimated the figure equivalent to this year's target of £8½ billion at around £11 billion; the equivalent of this year's likely outcome (which we have estimated at around £9 billion) * would be correspondingly higher.

However, the present high levels of interest rates, which are quite naturally most worrying to many businessmen, though largely the result of inflation are also partly due to the level of the PSBR in relation to the money supply limits. This is a strong argument for reducing the PSBR in real terms in the next financial year. As well as reducing the pressure of the Government's claims on funds in the financial markets, it would improve market sentiment and confidence in the Government's monetary policy and so help in this way also to reduce interest rates.

But this argument must not be pushed too far. Interest rates are expected to fall even on the assumption of no reduction in the Government's spending plans for 1980/81. ** If these plans are cut substantially as we have recommended (and Ministers have indicated that they intend to make substantial cuts), this will itself improve confidence and help to lower interest rates further. A judgment is thus needed on whether, and to what extent, the cut in Government spending plans should be accompanied by a reduction in the burden of taxation. As we explain below, there is a strong case for a number of important tax cuts - to increase incentives, to assist company finances, to remedy anomalies, and generally to keep up the momentum started in the last Budget.

Attention also has to be paid to the likely state of the economy over the coming 12-18 months. Our view, as explained earlier in these Representations, is that output and profitability will be falling and unemployment rising. Income tax cuts would limit the expected fall in spending power of individuals during the coming year and (allowing for some effect on imports) this would benefit sales and output and hence profits. In addition, the tax changes proposed below to help company finances generally, and in particular to encourage entrepreneurs and small firms, would have a similar effect.

Against these benefits to business finances must be set any adverse effects of interest rates being higher than they would otherwise have been as a result of a higher PSBR to accommodate the tax cuts. But we do not believe that these effects need be very great in relation to the benefits just mentioned, provided at least that the tax cuts are seen to be broadly balanced by reductions in Government spending, and provided the PSBR is seen to be on a falling trend as a proportion of GDP, after allowing for the temporary effects of the recession.

* See page 11 above

** See page 12 above

Taking all these factors into account, and assuming that our recommended cut of around £2 billion in the next financial year in government spending plans is to a large extent achieved, we propose below a package of reductions in direct taxation which would cost around £1½ billion in 1980/81. This is the minimum package which we believe to be urgently required. It would be likely to result in a PSBR of the order of the £10 billion which we forecast on existing policies *, and if anything a rather lower figure. It would, as explained above, imply a somewhat tighter fiscal stance than in the current financial year. It would be approximately the same proportion of GDP and consistent with a downward trend in this proportion allowing for the recession we expect in 1980/81.

If the Government were expecting a deeper recession and, solely as a result of this, a higher PSBR, it would be wrong to attempt to correct this automatically. As argued above, the PSBR should be adjusted for the effects of recession on government revenue and expenditure in determining whether the trend as a percentage of GDP is downward, although market psychology has also to be taken into account.

If our proposals on direct taxation would, on the Government's reckoning, result in a higher PSBR than we recommend, we would reluctantly accept some increase in specific duties, in order to help finance our programme of direct tax reductions. However, as we have emphasised elsewhere in these Representations, it is extremely important to minimise any adverse effects of the Budget on the price level.

* As mentioned on page 11 above, this is approximately at the centre of the range of other forecasts.

SECTION 7

TAX RECOMMENDATIONS

In the circumstances of the coming Budget, the tax priorities within a necessarily limited total cost, must be to increase the incentives to work, to relieve the financial pressures facing businesses, to reduce capital taxes and to encourage smaller firms in other ways.

PERSONAL TAX AND INCENTIVES

Once again we give high priority to reducing the level of personal taxation. Last year the Chancellor introduced substantial reductions in the burden of personal tax - reductions which CBI had long advocated. We welcomed these as the first step in bringing personal tax in this country down to a reasonable level.

The Chancellor, too, fully recognised the need for further reductions. In his Budget Statement he said:

'Excessive rates of income tax bear a heavy responsibility for the lack-lustre performance of the British economy. We need, therefore, to cut income tax at all levels. For the reasons I have already explained, I cannot do as much this year as I should have liked, and I cannot do as much as is needed. But, although it is only a first instalment, there should be no doubt in anyone's mind that this Budget marks a turning point'.

(Hansard, 12 June 1979, Col. 258)

As we have already said, the scope for tax reductions in the coming year is likely to be extremely limited. Nevertheless, it is imperative that the level of personal tax, particularly as it bears on individuals at the bottom end of the income scale, should be further reduced. Last year, all taxpayers benefited to some extent from the Chancellor's personal tax measures, but those in the lower income ranges did less well than the higher paid. The clear priority then was to reduce all income tax rates - and in particular the higher rates - to more reasonable levels but, now that some progress has been made in this direction, the Government must do more to help the lower-paid.

Personal allowances

The best way of doing this is to increase the tax threshold in real terms. The law requires personal allowances to be increased each year in line with inflation, and we assume that this will be done. We welcome this provision, as a partial solution to the problem of 'fiscal drag' at the starting point of tax.

But indexation of the threshold only prevents it from falling in real terms and, as the Chancellor recognised last year, this alone is not enough. In order to increase the net financial benefits of working, real increases in personal allowances are needed, over and above indexation. Last year the Chancellor estimated that his increases in the thresholds meant that some 1.3 million people who would otherwise have paid income tax would not do so. Even with this increase, however, the starting point for tax in this country still remains

very low compared with other countries, as Table 2 shows,

TABLE 2

THE LEVEL OF EARNED INCOME AT WHICH INCOME TAX
STARTS TO BE PAYABLE IN SELECTED COUNTRIES

	Income Tax	Initial
	Threshold	Rate
	£	%
France	4400	5
Italy	1200	10
Japan	3280	10
USA	3240	14
Netherlands	2910	20
Germany	3265	22
Ireland	2500	25
UK	1815	25

NOTES

- 1 Assuming a married man with 2 children.
- 2 Thresholds and rates are for the following tax years: France year beginning 1/1/79 charged on 1978 income; Germany, Netherlands, Italy, USA year beginning 1/1/79; Ireland and UK 1979/80; Japan year beginning 1/4/78.
- 3 The figures take account (where applicable) of personal allowances, minimum expense deductions, earned income reliefs and tax-deductible social security contributions.
- 4 Exchange Rates used are for 21/1/80.

Sources: European Taxation (International Bureau of Fiscal Documentation); Price Waterhouse Information Guides; US Federal Tax Guide (Commerce Clearing House); Guide to Japanese Taxes 1978/9 (Taizo Hayashi).

and this, combined with the high initial rate of tax, bears heavily on the lower paid. And, since last June, inflation will have brought many of these people back into tax. Moreover, cutting the number of taxpayers in this way will reduce the burden on the Inland Revenue and, therefore, the number of civil servants which the Revenue need to employ.

Increases in personal allowances are very costly in Budgetary terms, and we cannot therefore recommend as large an increase as we should have wished. Nevertheless, we recommend that personal allowances should be increased by about 7½% in real terms this year: this would take slightly more than half a million taxpayers out of charge and would increase incentives to work. We estimate that the cost of this proposal would be in the order of £900 million in 1980-81 and £1100 million in 1981-82.

The effects of our proposal on the burden of personal tax are shown in Table 3.

TABLE 3

EFFECTS OF CBI TAX PROPOSALS FOR 1980/1¹

Gross Annual Income	1979/80		1980/1 Unchanged Policies ³		1980/1 CBI Proposals ⁴	
	Tax ² Payable	Average Rate	Tax ² Payable	Average Rate	Tax ² Payable	Average Rate
	£	£ %	£	%	£	%
2250	255	11.3	179	8.0	152 ⁵	6.8
2500	334	13.4	258	10.3	218	8.7
3000	513	17.1	422	14.1	377	12.6
3500	696	19.9	606	17.3	558	15.9
4000	878	22.0	790	19.8	742	18.6
4500	1061	23.6	974	21.6	925	20.6
5000	1243	24.9	1157	23.1	1109	22.2
7500	2124	28.3	2076	27.7	2028	27.0
10000	2874	28.7	2899	29.0	2851	28.5
12500	3693	29.5	3685	29.5	3620	29.0
15000	4752	31.7	4728	31.5	4655	31.0
20000	7161	35.8	7121	35.6	7040	35.2
25000	9820	39.3	9764	39.1	9675	38.7
30000	12730	42.4	12656	42.2	12560	41.9

NOTES

- Calculations are for a married man (with or without children), wife not earning, with only basic personal allowances.
- Including social security contributions at the non-contracted-out rate. The proposed increase in the rate and threshold for payment of contributions has been included for 1980/1. It will be noted that the effect of this increase is that in 1980-81, on unchanged policies (ie assuming indexation of personal allowances at 18%), individuals earning £10,000 a year will actually be worse off, and those above that level only marginally better off.
- Assuming no personal tax changes except automatic increase of personal allowances by 18% in line with inflation.
- Assuming a 7.5% increase in personal allowances after indexation for inflation as in 3.
- The £152 shown as tax payable is entirely payment of social security contributions. No income tax would be payable under the 1980/1 CBI Proposals until an income of £2300 is reached if only the main personal allowances are taken into account. Under the column headed 1980/1 Unchanged Policies, tax would become payable, assuming again only basic personal allowances, at an income of £2142.

Additionally, real increases in personal allowances could be achieved at a much lower cost to the Exchequer by a comparatively simple change in the personal tax system. If the lower rate band of income tax (whereby the first £750 of taxable income is taxed at 25%) were to be abolished, the main personal allowances could be increased in real terms and the basic rate band widened in such a way that no taxpayer - whatever his income - would be adversely affected, but only those taxpayers whose taxable income was less than £750 a year would benefit. Such a proposal would take about half a million people out of the tax net, thereby concentrating help where it is most needed. We estimate that the cost of doing this would be relatively low - of the order of £100 million.

Basic rate of tax

Our medium-term objective continues to be a basic rate at a more reasonable level than the present 30%, and we were therefore gratified to note that this is also the Chancellor's aim. Ideally, this year we should have liked to see further substantial progress towards his target of 25% - not least because reductions in the basic rate are the most cost-effective means of reducing the tax burden on middle-managers. Although, for the reasons given above, our first priority must be to achieve increases in personal allowances, the tax position of middle-managers remains a matter of great concern to us. In general, this group benefited less overall from the June 1979 Budget than many others; and their position since then has deteriorated as a result of the increases in interest rates and in particular, mortgage interest. This is why we stress below that no immediate increase should be made in the taxation of company cars; furthermore, we urge that other aspects of taxation which impinge particularly on this group should be reviewed. (For example, limits applying to tax relief on mortgage interest and to stamp duty - particularly as it applies to houses should be increased.

Higher rates of income tax

Last year the Chancellor made substantial reductions in the higher rate tax burden, broadly in line with our recommendations. We hope the Government will implement our recommendations in full as soon as possible, by reducing the top rate to 50%, and by further widening the higher rate bands. For this year, however, we do not believe that any progress can be made towards these objectives, although we urge the Chancellor to give a firm commitment for future years to the annual indexation (taking 1979 as the base date) of the starting points for all rates of tax, in order to avoid increases in the real tax burden on middle and senior managers through inflation. The Government has apparently accepted the principle of automatic revalorisation of the starting point for tax: this proposal merely continues this principle in relation to the starting points for the higher tax rates.

Investment Income Surcharge

The reduction in the burden of IIS last year was very welcome, and particularly benefited the smaller investor. Nonetheless, this surcharge remains a substantial disincentive to invest. It would of course be relatively easy to reduce the burden of IIS still further; but we believe that the Government should take the positive step of abolishing IIS once and for all. We estimate that the cost of this proposal in the coming year would be about £35 million and about £225 million in 1981-82.

Benefits in Kind

Last summer, in the wake of the June Budget, the Government announced plans to review the tax treatment of benefits in kind. Shortly afterwards, the Inland Revenue issued a consultative document proposing changes in the tax treatment of cars and petrol.

We have already commented separately on the details of the Inland Revenue's proposals. In principle, we support the Government's objective of removing the fiscal advantage of paying in kind rather than in cash. We believe that employers should be free to arrange with each of their employees whatever remuneration package is the most appropriate and that this decision should not be inhibited by tax considerations. However, we have three major comments on the approach which the Government has apparently adopted towards this question.

Firstly, there must be no substantial changes in the tax treatment of benefits in kind until the Government succeeds in its aim of reducing personal tax to a reasonable level all the way down the income scale.

Secondly, the Government must adopt an even-handed approach to this question. It is quite wrong to single out cars and petrol for major increases in tax without also reviewing the taxation of other benefits, many of which clearly have less commercial justification than cars.

Finally, full account must be taken of the likely effects on industry of fundamental changes in the taxation of some benefits. In the case of cars, the UK motor manufacturing industry could be adversely affected unless there is a suitable transitional period before major changes take effect.

We therefore urge the Government in the strongest terms not to propose any increases in the taxation of cars this year.

Profit Sharing

The CBI attaches a great deal of importance to improving communications and increasing employee involvement; in particular, we share the Government's clear desire (as expressed in the Conservative Manifesto 1979) to expand and build upon existing schemes for encouraging employee share-ownership. In principle, we welcomed the tax reliefs for profit sharing schemes introduced in the 1978 Finance Act as a helpful first step. But, as we pointed out in May last year in our representations to the incoming Government, schemes implemented under these provisions were likely to be limited to those companies who would be capable of coping with the administrative complexities of the legislation. We recommended that the 1978 provisions should be made less restrictive and should allow greater flexibility, so that firms could choose whatever scheme was best suited to their individual requirements.

Our views on this subject remain unchanged. It is now apparent that only a relatively small number of firms has sought to introduce profit-sharing schemes in the light of the 1978 provisions, largely because these provisions are not sufficiently flexible and are administratively too complicated. We believe that the system should be simplified; in addition, the rules could be made less restrictive if the period of ten years during which an employee cannot sell shares without incurring an income tax liability were to be reduced to five years and if the period during which shares could not normally be sold at all were to be reduced from five years to one year. The Government should also increase the present annual limit of £500 on the value of shares that may be assigned to each employee to £1000.

CAPITAL TAXATION

The CBI welcomed the Chancellor's assurance in his Budget Statement last year that the Government 'were determined to make the taxation of capital simpler and less oppressive'. We wholeheartedly endorse this statement, having been convinced for a long time that capital taxes - and in particular capital transfer tax (CTT) and capital gains tax (CGT) - are substantially harmful to businesses.

The Chancellor announced that Treasury Ministers would undertake an immediate review of these taxes. Subsequently, in October 1979, the CBI presented a detailed submission to the Chancellor proposing what we consider to be essential changes in the rules governing CTT and CGT for implementation in this year's Finance Bill.

The main impact of capital transfer tax, in a business context, is on the small and on the expanding family firm. In many ways it is a directly regressive tax on company success because the principal shareholders will be unable to meet the CTT liability out of ready income. All too often the only remedy will be to sell the company concerned, with a consequent loss of family interest and therefore, momentum. In his Budget Statement last year, the Chancellor identified the crucial issue when he referred to the desire of an individual to build up capital and pass it on to his children. In the case of the family firm, it is vital that an individual should be able to do this without having to take steps that would impair the continued existence of his business. Table 4 compares the CTT position in the UK and in some important EEC countries.

TABLE 4

**STARTING AND MAXIMUM RATES OF CAPITAL
TRANSFER TAX (OR EQUIVALENT) IN SOME EEC COUNTRIES
ON BEQUESTS¹ FROM PARENTS TO THEIR CHILDREN²**

	Starting Rate	Threshold ⁴ £	Maximum Rate	Threshold ⁴ £
UK ³	10	25,000	75	2,010,000
Belgium	3	7,800	17	164,000
France	5	18,900	20	29,750
Germany	3	22,800	35	25,300,000
Ireland	25	150,000	50	400,000
Italy ³	3	16,300	31	543,800

NOTE:

- 1 Most of the countries have different rules for lifetime gifts.
- 2 All countries shown, except the UK, impose a different (usually higher) tax burden on bequests to some or all people other than the children of the donor.
- 3 In Italy and the UK, the rates and thresholds shown apply to the entire estate of the deceased. In the other countries shown they apply to receipts by the inheritors.
- 4 The exchange rates used are for 21/1/80.

Sources: Price Waterhouse Information Guides; OECD Report on the Taxation of Net Wealth, Capital Transfers and Capital Gains on Individuals.

The most objectionable feature of capital gains tax is that it is so rarely a tax on capital gains. If it was charged on real gains as opposed to increases in monetary values, we believe that only minor changes would need to be made to its structure. The logical way of ensuring that only real gains are taxed is by the indexation of the acquisition cost, to reflect the fall in the purchasing power of money between acquisition and disposal.

Tapering is a practical alternative to indexation - although it is not so relevant to inflation, but rather to the argument that the longer an asset is owned, the less should be the tax on the eventual gain. Thus, tapering does not necessarily eliminate any inflationary element of a chargeable gain - it may however have that result.

The proposals which we submitted in October last year were aimed at alleviating as far as possible the harmful impact on business of these two taxes. For capital transfer tax, we urged the Chancellor to give careful consideration to outright abolition of the tax. Failing that, we proposed a substantial increase in the starting point from £25,000 to £50,000 and a rationalisation and widening of the rate structure, so that the top rate of 50% should not apply until the value of the property transferred exceeded £3 million (as opposed to the present 75% on property worth over £2.01 million). We proposed that the rates applicable to lifetime transfers should be half those on bequests all the way up the scale, and we recommended the introduction of consanguinity relief, of not less than half rate, for transfers to lineal descendants (in line with European practice). Likewise, we recommended that a similar relief should be available for gifts to full-time employees of a business owned in whole or in part by the donor. For capital gains tax, we advocated either indexation or tapering in respect of assets owned for seven years or less but, on either basis, no tax charge at all on assets owned for more than seven years. We also included in our submission several detailed proposals relating to both these taxes.

In making these recommendations we were aware that, although their cost in 1980-81 would be relatively low, the gross cost in later years would be much higher. It is of course notoriously difficult to produce even approximate costings for changes in capital taxes; but, with this qualification, we estimate that the first year cost of the package submitted last autumn could be in the order of £150-200 million but that the gross cost in later years could be about £600-700 million, if not more. Most of this cost is derived from the substantial increases which we propose in the starting point and thresholds at the lower end of the CTT rate structure and the indexation or tapering of CGT.

We believe that our proposals should be implemented in full this year. However, if the Chancellor decides that the scope for direct tax reductions in the short-term is limited and that he must therefore introduce his capital tax reforms in stages, we outline the proposals from our October 1979 submission to which we give the highest priority, as these would provide maximum relief for the business sector, while costing much less in full year terms than our full package. But our full October package remains our firm objective, and we look for an assurance from the Chancellor that he will implement the rest of our recommendations at an early date.

For capital transfer tax we recommend, in addition to a significant increase in the starting point and reductions in the rates (particularly of the punitive top rates), the following detailed proposals to help the owners of family firms:

- i The continuation of the existing reliefs for business, agriculture and woodlands. In the case of businesses, however, the 50% relief should be extended to all business assets and interests.

- ii The abolition of the principle of life-time cumulation. We believe that cumulation should only apply for a limited period, say seven years, and that the tax rates applicable to life-time transfers should be half those on bequests.
- iii The provisions for payment by instalments should be improved: the £250,000 limit should be abolished, and in all cases interest should only run on instalments not paid by the due date.
- iv The donor's annual exemption limit should be increased from £2,000 to £10,000 and the annual exemption per donee from £100 to £1,000.
- v The 'related property' provisions should be reformed. The present law requires that business interests (particularly shares) may be valued for CTT purposes at a higher figure because they are to be aggregated with other interests in the same business. These provisions should be made less harsh.
- vi The periodic charge on settlements in which there is no interest in possession should be abolished.
- vii The various thresholds and fixed sum exemptions should be adjusted in line with inflation each year.

For capital gains tax, we look for a reduction in the standard rate to 25% and some increase in the exempt threshold. Moreover, we remain strongly committed to a reform of capital gains tax to take account both of the effect of inflation on chargeable gains and of the principle that the tax should not be charged on assets held in the longer term. We urge the Chancellor to give high priority to both these points. We also advocate the following detailed changes:

- i The extension of the present 'rollover relief' to all productive assets.
- ii The abolition of CGT on life-time gifts in order to eliminate the considerable problems currently produced by the unsatisfactory interaction between CGT and CTT.
- iii A thorough overhaul of the retirement relief provisions which provide help for individuals of retirement age who dispose of their business assets.
- iv The removal of the double charge where assets are held through a company which goes into liquidation. In such cases, the company should not be taxed on the disposal of its assets: the only liability should arise when the shareholders dispose of their shares.
- v Movable tangible assets which are wasting assets but which qualify for capital allowances (eg tractors) should be exempt from the tax.
- vi The provisions for payment by instalments (and for any interest charge) should be the same as those for CTT.
- vii The various thresholds and fixed sum exemptions should be adjusted in line with inflation each year.

As we have said, we regard these proposals as the bare minimum for immediate implementation this year: we emphasise that they cannot in any way be regarded as an alternative to the capital taxes package outlined in our October 1979 submission.

SMALLER FIRMS

As an organisation, we recognise the importance of the smaller firms sector to the British economy as a whole. Smaller firms are frequently important sources of innovation, and they provide essential services to larger firms as suppliers of parts and components. They contribute to the maintenance of competition and the proper workings of a mixed economy: many believe that over the next few years this sector is likely to contribute most to the creation of new jobs.

However, it is likely that during this period, even more than most businesses, smaller firms will experience considerable financial difficulties. Unless something is done to help them, many will go out of business; and, equally damaging for the economy, many will never get started. Despite the help given in recent years to smaller firms, the system is still weighted against them.

For these reasons, the CBI attaches very high priority to measures designed specifically to assist smaller firms and, in particular, to helping them to overcome the difficulties they experience in obtaining sufficient equity finance in their early years (largely because other forms of investment eg gilt-edged securities are more attractive, partly because of preferential tax treatment).

We believe that, despite the risk of further complicating an already complex tax system, the Government should introduce measures specifically designed to increase the incentive of private individuals to invest in new and developing businesses. To this end, the following possibilities should be urgently reviewed:

- i A deduction against an individual's personal tax for investment in smaller firms (possibly on the lines of the 'Loi Monory' recently introduced in France)
- ii A 'Special Investment Reserve Fund' which would allow a tax exemption for income placed into such a fund for future investment in a new firm. (This would help salaried employees who wish to set aside funds in order to start up their own businesses.)
- iii A deduction against a shareholder's personal tax for bona fide losses incurred by small companies in which he has invested. (At present, such a relief is available only for partnerships and sole traders.)
- iv 'Small Firm Investment Companies' (on the lines set out in the Interim Report of the Committee to Review the Functioning of Financial Institutions) would provide a valuable source of finance for smaller firms. The creation of such intermediaries could be encouraged by personal tax reliefs for individuals who invest in them.

In addition, many of the recommendations elsewhere in our Representations would also provide considerable help to the smaller firms sector (in particular, our capital tax proposals; the proposed increases in the profit limits for the lower and marginal rates of corporation tax; the abolition of Investment Income Surcharge and the close company apportionment provisions).

CORPORATION TAX

The Government are currently reviewing the present system of corporation tax, and one major aspect of their review will concern the role of capital allowances and stock relief. In his Budget Statement last year, the Chancellor said that the tax system should take account of the effects of inflation on businesses, and that it should do so in a way that is reasonably objective, equitable and simple to administer. At the same time, however, he made it clear that no changes in the system of company taxation would be proposed without careful consultation in advance.

In the light of this welcome assurance, we assume that the Government will not be proposing any substantial changes in the present system of corporation tax in the forthcoming Budget. We firmly believe that stability in the tax system will be one of the most important factors in helping business to get back on its feet again. It would be particularly damaging to make fundamental changes in the taxation of companies during a period of recession.

In our Technical Budget Representations in Part II of this paper, we list a number of important changes which should be made in the rules governing Advance Corporation Tax (ACT). Otherwise we have no major recommendations on the structure of the tax at present.

So far as the rates of corporation tax are concerned, the financial position of companies continues to cause very great concern, even with the assistance given by stock relief and capital allowances, and in other circumstances we should be looking for a reduction in the rates to leave more money for expansion and investment. Given our Budget judgment, however, we propose no reduction in the actual rates although we believe that the limits for the reduced rates should be increased again this year to take account of inflation. This would be a comparatively inexpensive measure, and would particularly help smaller companies.

Stock Relief

We welcomed the improvements made last year to the present system of stock relief, although not all of our recommendations were implemented. In view of the considerable financial difficulties which very many companies have encountered, we urge the Government to implement our remaining recommendations: that the six year 'write-off' period should be reduced to four years; that companies which make partial claims for relief should be able to carry forward the unclaimed proportion of the relief; and that there should be provisions to deal with temporary reductions ('dips') in stock. In particular, 'dips' are likely to cause serious problems as a result of the steelworkers' strike and we recommend that our proposal should apply for financial year 1979, and later years.

With these essential improvements, stock relief will continue to be broadly satisfactory until an acceptable form of inflation accounting has been introduced and tested. In the meantime, however, we should draw the Chancellor's attention to the dangers that would follow from any attempt to make the present system any more restrictive than it is.

Close company apportionment provisions

The present apportionment provisions relating to close companies were introduced largely in order to counter tax avoidance. With marginal rates of income tax rising to 83% (98% in the case of investment income) there was some justification for retaining these complicated and troublesome provisions despite the small amounts of revenue which they produced. However, the top rate of tax on earnings has been reduced to 60% and, if our proposal to abolish IIS is implemented, this would also be the maximum rate applicable to investment income. Whether or not IIS is abolished, we believe that the case for retaining the close company provisions has all but vanished, and we recommend that they should be abolished forthwith. This worthwhile simplification in the tax system would save a great deal of inconvenience to both taxpayers and the Inland Revenue, and the Revenue cost would be very small.

NATIONAL INSURANCE SURCHARGE (NIS)

We remain as strongly opposed as ever to the National Insurance Surcharge. We have repeatedly stressed the very damaging effects which it has on the economy: it reduces employment, because it makes it more expensive for employers to take on new labour; it worsens the balance of payments, because it is charged on exports but not on imports; it increases prices (after a short delay) because it is a labour cost; and it squeezes profits, with harmful effects on investment.

The rate of employer's National Insurance contributions, including the Surcharge, will be 13.7% from 6 April 1980 (not contracted out). This compares most unfavourably with the level of 8.75% in March 1977.

In past statements, the Chancellor of the Exchequer has recognised the folly of making any further increase in the Surcharge. We urge him to go one step further now by giving a firm undertaking to abolish NIS, beginning as soon as possible.

INDIRECT TAXATION

In his Budget last year, the Chancellor made a substantial shift in the tax burden from direct to indirect tax. This is broadly in line with the policies that we have been recommending for some time now. We have argued, however, that this shift should ideally be achieved by reducing personal tax rather than by increasing the real burden of indirect tax, although in last year's Budget Representations we reluctantly accepted that some increases in indirect tax might be necessary to free the resources needed to make the essential and long overdue cuts in income tax.

This was the course which the Chancellor adopted last year although, in increasing the VAT rate to 15%, he went further than we suggested. For this year, however, we believe that if possible the Chancellor should avoid any further indirect tax increases. We therefore welcomed the suggestion by Treasury Ministers during last year's Budget debates that they would not propose any higher rate of VAT. And, while inflation remains at such a high level, we would not advocate any increase in specific duties although we would accept that increases are likely to be necessary at some future stage.

PRIORITY TECHNICAL REPRESENTATIONS

Once again, we have selected a few of our technical representations as having particular priority. We have already discussed these with Inland Revenue officials, but we believe that they are so important that we would like to draw them to the Chancellor's attention. There are five main points:

i Disallowed Business Expenses

All expenses incurred for bona fide business purposes should be allowed for tax. The Government have accepted this principle to some extent in publishing proposals to extend tax relief to certain costs of business loan finance. We welcome this as a first step, although it is very limited; but we look to the Chancellor for measures to relieve all disallowed business expenses.

ii Exchange profits and losses

Exchange losses arising from foreign currency transactions should be allowed for tax. We entirely accept the natural corollary that profits from such transactions should be taxable.

iii Commercial buildings allowances

It is a major anomaly that capital allowances should be available for industrial buildings and hotels but that no relief at all is given for expenditure on commercial buildings. A start, however limited, should be made in extending allowances to these buildings.

iv Consortium group relief

The present loss relief provisions for companies involved in a consortium are unduly restrictive, thereby inhibiting projects financed in this way. The provisions should be brought more into line with the present rules governing tax relief for losses within a group.

v Group relief for capital losses

The present tax law prevents companies from surrendering capital losses to other companies within their group. As a result, much unproductive work is carried out in transferring assets between group members in order to match gains with losses. These difficulties should be eliminated by permitting capital losses to be freely transferred within a group.

BUSINESS RATES

There is widespread concern in business, given the difficult financial position of companies, about the substantial rate increases that have been announced for 1980-81 in many areas. These increases average over 20% and rises of 30% or more are not uncommon. Nearly half of local authorities rate receipts are paid by industry and commerce and they amount to considerably more than half the yield from corporation tax.

This burden is already too heavy and the Government should take steps to safeguard businesses from excessive rate demands, including those that may arise for 1981-82 as a result of the change in rate support grant system. While we support the proposed reform of rate support grant as a means of discouraging excessive expenditure by local councils, we are concerned that it may lead to further very large increases in rates levied by authorities intent on implementing unrealistic expenditure plans. One possible way to protect business would be to limit business rates to a maximum poundage which corresponds with the so-called 'common standard' plus the defined threshold. Thus the burden of high spending over and above the common standard would fall on the domestic sector which, unlike the business sector, has democratic representation.

Looking further ahead, the CBI remains opposed to the derating of domestic properties if as a consequence this means that the burden of local government finance borne by the business community will increase.

OTHER TAX PROPOSALS

a Development Land Tax (DLT)

Although the Chancellor, in reducing the burden of this tax last year, announced that he had no plans to abolish it, we continue to see very little case for its retention, particularly in view of its minimal yield. The tax is cumbersome, extremely complicated and uncertain in its incidence; and its interaction with other taxes is very unsatisfactory. In our technical Budget representations, we propose a number of detailed improvements which could be made to the present rules but we believe the best and most logical step would be to abolish DLT outright and we urge the Chancellor to review this matter once again.

b Taxation of Social Security Benefits

It is clearly anomalous that some social security benefits are subject to tax in the same way as other sources of income, whereas other benefits are not. This has not always been the case; and the anomaly exists not through any point of principle, but for administrative convenience. We therefore welcome the review of this question currently being undertaken by the Government.

FURTHER PRIORITIES

The foregoing assumes that only about £1500 million will be available in 1980-81 for tax reductions. If greater scope than this exists, our priorities for further action (not necessarily in this order) would be as follows:

- immediate action to adjust the starting points for all personal tax rates in line with the 'Rooker-Wise' increases.
- reduction in the rate of National Insurance Surcharge.
- reduction in the basic rate of income tax.

SUMMARY

The following table summarises the CBI proposals for reductions in direct taxes:

	Cost (£m) 1980-81 (round numbers)
7½% <u>real</u> increase in personal allowances (over and above statutory adjustment for inflation)	900
Capital tax proposals (full CBI October 1979 recommendations) and abolition of IIS and DLT	200
Improvements in stock relief	300
Reliefs for smaller firms, priority technical representations, etc	100
	<hr/> 1500

Note

The table gives estimated costings for 1980-81. The cost of these proposals in 1981-82 and later years would generally be higher (and, in the case of our capital tax proposals, much higher). Thus, in a full year the 7½% real increase in personal allowances would cost in the order of £1100 million (in 1980-81 terms). The capital tax proposals, including abolition of IIS and DLT, could in gross terms cost £800 - 900 million in a "full-year" but would be less in 1981-82, to an unknown extent; our priorities within this package are indicated in the text. The cost of the improvements in stock relief would be about the same in 1981-82 (because we recommend these should be backdated). The reliefs for smaller firms and our priority technical Budget representations might cost about £200-300 million in 1981-82, and rise gradually over a long period of years as more new commercial buildings qualify for capital allowances.

Part II

Technical representations

SECTION 1

INTRODUCTION

This part contains the CBI technical Budget representations for 1980 which were first submitted to the Government in November of last year. It is arranged as follows:

REFORM OF LEGISLATIVE PROCEDURES

This section outlines the main defects of the existing procedure by which tax provisions are drawn up and enacted and examines a number of possible improvements.

PRIORITY BUDGET REPRESENTATIONS

We have selected five proposals as the ones to which the CBI attaches the greatest priority. The first four were priority representations for 1979, and the need for urgent action on these points has in no way diminished in the past 12 months. The fifth was included in our main list of representations for 1979. We regard each of these proposals as having the same priority.

Our five priority representations - each of which raises an important question of principle and is much more than just a technical point - are as follows:

- i Disallowed business expenses;
- ii Capital allowances for commercial buildings;
- iii Exchange profits and losses on foreign currency borrowings;
- iv Group relief for consortium companies; and
- v Grouping of capital losses.

OTHER TECHNICAL REPRESENTATIONS

This section of our submission lists the main technical representations which, although of rather more detailed application than our priority representations, are nevertheless matters on which action must be taken as soon as possible. A number of items have been omitted from this list because, although important, they are unlikely for one reason or another to be favourably received by Government at present. But we reserve the right to return to these matters in the future.

Our representations do not include our proposals for capital transfer tax and capital gains tax. These have been set out in a separate submission which was sent in October 1979 to the Chancellor of the Exchequer. Other matters - such as the taxation of cars and petrol as benefits in kind - have also been the subject of a separate submission.

SECTION 2

REFORM OF LEGISLATIVE PROCEDURE

In a speech to the Addington Society on 16 February 1977 - made when he was in Opposition - the Chancellor of the Exchequer, Sir Geoffrey Howe, stated:

"We need a radical reform of our machinery of tax legislation. Only then will the legislation itself become intelligent and intelligible."

Sir Geoffrey's speech was a masterly critique of the present legislative process. He identified many weaknesses about which the CBI and other representative bodies had long been concerned, and he put forward a number of proposals which, he felt, would go a long way towards solving these problems.

DEFECTS OF THE PRESENT LEGISLATIVE SYSTEM

In normal circumstances, work on a Budget by the Inland Revenue and the other Government departments involved begins in the September before the scheduled March or April date. Often to a strict timetable, the work on suggested items for the Finance Bill, the selection procedure and the drafting of the legislation is carried out in an atmosphere of 'Budget Secrecy', whether or not the material under consideration is inherently secret. This secrecy, however, effectively prevents any substantial consultation with the people who are most likely to be affected by the proposals: the firms or individuals who have to pay the tax, and the practitioners who have to find their way through the labyrinthine legislation.

After the Budget and the publication of the Finance Bill, the Parliamentary timetable is fixed without any particular regard to what might be needed to ensure that the final product is the right one. Countless amendments to the Bill are tabled; most have the aim of changing the law or the Government's proposals but some are designed only to elicit the purpose behind a particular provision in the Bill. Only a small percentage of the amendments tabled are selected for debate, but even so there is scarcely sufficient time to give adequate consideration to the ones that are called - which may raise issues of fundamental importance. Even if a full debate is possible on an important point, it all too frequently takes place in the early hours of the morning. In these circumstances, it would be very surprising if our tax law was not riddled with errors and loopholes.

As Sir Geoffrey commented in his speech:

"During the whole weary, yet far too hasty, procedure, there has been far too little opportunity for outside experts - lawyers, accountants, industrialists - to give the benefit of their advice, either on the broad economic measures or the practicality of operating the more detailed provisions. Before the Bill is published, they have little or no chance of being heard; and after the Bill is published, there is scarcely time to heed their advice."

POSSIBLE REMEDIES

We have directed our attention towards the two fundamental aspects of this problem: firstly, the lack of proper consultation with those most likely to be affected by the proposed legislation and, secondly, the lack of Parliamentary time and Finance Bill space to deal with the many technical anomalies in the tax system.

In his speech Sir Geoffrey rejected - in the CBI view, quite rightly - a 'root and branch' reform of the tax system as a solution to the problems caused by these defects in the legislative process. Such an undertaking would be a major one, and while we would not necessarily reject out of hand the idea of a Royal Commission on the tax system, the CBI would certainly endorse his view that any reform of our present taxes must come only after full consideration and public consultation, something which cannot be achieved overnight. More importantly, it would not prevent any reformed system from falling into disrepair over time through the continuing defects of the legislative procedure.

The same considerations do not, however, apply to reforms of the legislative procedure. If properly considered and carried through in practice, effective changes in that procedure should, over a period of time, have a beneficial reforming effect on the whole tax system. In recent years, several possibilities have been canvassed at one time or another. The proposals which, in our view, merit the most serious consideration are as follows:

The use of Select Committees on Taxation

Last year, the Government announced proposals to establish a number of permanent Select Committees, one of which would have responsibility for matters affecting the Treasury, Inland Revenue, Customs and Excise and the Civil Service Department. It is not clear at this stage to what extent this Committee will in future seek to involve itself in tax matters.

In general, however, we would favour the use of a Select Committee - whether a standing or an ad hoc one - only on major tax proposals, such as those preceded by a Green Paper. In recent years the Select Committee established to consider the reform of Corporation Tax was extremely successful, and in our view, demonstrates the right use of Select Committees in the taxation field. We should be surprised, therefore, if this new committee were to involve itself on a regular basis in minor technical tax matters. These should be dealt with by other changes in the legislative process.

Pre-Budget consultation

We welcome the fact that the need for the fullest possible consultation on major tax changes - with the publication of Green or White papers - is now widely accepted. Consultation on lesser points by the Inland Revenue in recent years has become far more general and we take this opportunity to acknowledge this development. Nevertheless, there is still room for further improvements in the consultative process: too often, for one reason or another - whether lack of Finance Bill space, cost or otherwise - no action results from the consultation. We would agree with the Chancellor when he told the Addington Society that "consult now and draft later" should be the first motto of any Chancellor and that "there should be very few occasions on which this rule had to be disregarded in favour of the so-called need for Budget secrecy".

There are two main proposals for improving the existing pre-Budget consultative machinery. Some commentators have favoured the more formal approach of an annual consultative document, published in the late autumn or early winter, and outlining all the proposals in the forthcoming Finance Bill which do not affect tax rates and conjunctural matters. Others would prefer a less institutionalised system based on the Revenue's current practice, with consultative documents on specific proposals being published on an ad hoc basis.

In February 1977, when we last made proposals for a reform of the legislative process, our preference on balance was for a single consultative document. In theory this idea continues to be very attractive. However, we accept that this suggestion would give rise to serious practical difficulties. One of the main problems would be the task of fitting in yet another stage into an already crowded pre-Budget programme. To be of any value, such a document would normally have to be published by December at the latest - so that representations could be prepared, submitted and acted upon before the publication of the Bill.

Not only would that create additional pressure within the legislative procedure, but it would also impair the flexibility that a consultation process should have to be of maximum effect. Certain measures, for example changes in PRT, only affect a small number of taxpayers, others affect the majority and there are many which fall in between. Any consultative procedure must be sufficiently flexible to deal with the point at issue in the best possible way.

Because of these difficulties, we have concluded that a single consultative document before the Budget is not the best means of achieving our ends. We believe, however, that an alternative solution can be found in an extension of the present practice, whereby the Inland Revenue publishes consultative documents dealing with specific proposals on an ad hoc basis. In recent years, as we have acknowledged, this practice has become more commonplace and we believe that both the CBI and the Inland Revenue have gained from the airing which important issues have thereby received.

Such a procedure is flexible: it does not form part of the Budget timetable and is not therefore subject to the constraints that that imposes. It enables the Inland Revenue to issue the document whenever it is ready and to discuss the issues raised with those taxpayers most likely to be affected and their representative bodies, while at the same time offering the opportunity for others to comment.

In following this course, however, we believe that certain criteria should, wherever possible, be met. Firstly, to be of any value it is essential that those to whom a consultative paper is addressed should have ample time to consider and respond to the issues raised; in particular, representative bodies should be allowed sufficient time to consult their members on specific proposals and to formulate their reply. If necessary, they should have the chance to discuss important issues with officials before these proposals are enacted. Consultation in this way might impose a greater burden on officials but the additional time spent at this stage in ironing out discrepancies and anomalies will be more than repaid later on.

The consultation should in general be open to everyone, with formal publication of the documents, even if particular taxpayers or organisations are specifically approached for their comments. We accept, however, that in certain cases it may not be possible to give full publicity to such documents, if for example this might lead to widespread avoidance. Such cases would, we hope, be few in number. Finally, we believe that wherever possible and appropriate proposals embodied in such documents should be accompanied by draft legislation. It is to this particular aspect of consultation that we now turn.

Publication of draft legislation

In some cases, where the Government is clear in its own mind what it hopes to achieve, details of the draft legislation should be included in a discussion document. At other times, where the question is more open, this may not be possible; nevertheless, in such cases it would still be helpful to all concerned if, after the initial consultation process, draft clauses and schedules could be published as soon as they have been prepared and without awaiting the formal publication of the Finance Bill. The additional work which this would impose on officials and representative bodies before the Budget would be outweighed by the time saved when the Finance Bill came to be considered by Parliament.

If purely technical points arising from proposed legislation could be dealt with in advance, there would be more time during the legislative process to consider the actual implications of the proposals themselves.

A "Taxation" Bill

In February 1977 we urged the Government to introduce a separate Taxation Bill, dealing with purely technical matters. The present tax laws are riddled with minor anomalies and inconsistencies and the Inland Revenue have accepted in principle that many of these should be corrected. Space in the Finance Bill is however always at such a premium that these small points get pushed out by more important or urgent matters. A separate Taxation Bill from time to time would deal with these points: for the most part it would be uncontroversial, and we would not envisage a difficult passage for it through Parliament. The problem is simply one of allocating Parliamentary time to it every few years.

We would not envisage that such a Bill would eliminate the need to deal with some technical matters in the annual Finance Bill. Indeed, a separate Taxation Bill would be necessary on far fewer occasions as the standard of Finance Bill legislation rose as a result of our suggested improvements in the consultative procedure.

Sir Geoffrey acknowledged - and we would accept it as true - that even with the most efficient legislative procedure, mistakes would still occur from time to time. With this in mind, he repeated a recommendation made by the Renton Committee in 1975 to deal with such discrepancies. This was for a statutory committee of Revenue law experts who could put forward proposals for amendments to correct anomalies and other defects in the tax law. Proposals which did not change the purpose of the statute could then be included as a schedule to the Finance Act.

Such matters as would fall within this category might not however, cover as broad a spectrum as those as which would be dealt with by a technical Taxation Bill. We would accordingly give priority to establishing such a Bill as a regular, but not necessarily as an annual, feature of the legislative process. However, we also invite the Government to give further consideration to this proposal of the Renton Committee.

CONCLUSION

We welcome what the Chancellor of the Exchequer has said on the matters dealt with in this part of our representations. We believe that his speech to the Addington Society remains as relevant today as it was in 1977. A very strong case still exists for the reform of the legislative procedure and we have identified those proposals which we favour.

SECTION 3

PRIORITY TECHNICAL REPRESENTATIONS

As stated in the Introduction to this submission, there are five priority representations on which we wish to see action in 1980.

DISALLOWED BUSINESS EXPENSES

The provisions in the Taxes Act governing the computation of trading profits do not specify what types of expenditure may be deducted for tax purposes. Instead they seek to disallow certain expenses. As a result the main provisions continue to be the subject of substantial litigation. In many cases the main question at issue is not whether the expenditure was incurred for legitimate business purposes: that is common ground. The question is whether it was incurred for the purposes of an identifiable and continuing trade or whether it was of a revenue nature.

Thus, many legitimate business expenses do not qualify for any form of tax relief. Much of this disallowed expenditure is of crucial importance to new and expanding businesses: for example, expenses incurred prior to the commencement of trading and the expenses of raising and maintaining the finance to ensure that the business is properly capitalised. Businesses seeking new and better ways of conducting their trade may also be handicapped by the disallowance of, for example, the cost of abortive capital projects or of feasibility studies and payments to terminate onerous contracts. The recent case of *Tucker v Granada Motorway Services Limited* amply illustrates this final point: in this case a payment by a business tenant to a landlord to alter an onerous lease was disallowed for tax purposes.

The question of 'Nothings' has been the subject of detailed review by the Inland Revenue over a number of years. We therefore welcomed the publication last year of a consultative document on this subject. Our response to this document contained a number of detailed comments, but the main point about these proposals was that they only related to one aspect of this problem - the cost of raising loan capital. Many other aspects have still to be dealt with.

In a world where businesses need every encouragement to compete effectively, now is the time to tackle this problem with legislation which will permit as a deduction all bona fide expenses incurred by a person in his business.

CAPITAL ALLOWANCES FOR COMMERCIAL BUILDINGS

We make no apology for repeating this representation. An increasing proportion of new employment will be provided by the commercial and services sectors of business rather than industrial or manufacturing business. It is anomalous that an important sector of the economy should be at a disadvantage because expenditure on an essential asset such as its business premises does not qualify for a tax allowance. In paragraph 682 of its report, the Sandilands Committee saw no reason why commercial buildings should not qualify for capital allowances. As the Committee pointed out, this view was supported as long ago as 1951 by the Committee on the Taxation of Trading Profits, and again in 1962 by the Radcliffe Commission.

Successive Governments have accepted the argument in principle, but have claimed that the cost of the proposal would be too high. We accept that it would be costly, although the precise revenue loss would depend upon the measure of relief given. But we are convinced that this cost would to a large extent be offset by the stimulus that would be given to these sectors and by the increase in activity in the construction industry, which has been badly hit by past economic difficulties. A start, however modest, should be made at once. We therefore recommend that capital allowances should be given for all expenditure incurred on new commercial buildings which do not otherwise qualify, in the form of an initial allowance of 8 per cent and a writing down allowance of 8 per cent per annum.

EXCHANGE PROFITS AND LOSSES ON FOREIGN CURRENCY BORROWINGS

Following the Budget Statement in 1976, an Inland Revenue consultative paper considered the possibility of tax relief for losses on foreign currency borrowings. No steps have been taken since then to introduce such a relief. Despite the fact that sterling has appreciated in value over the past few years, we believe that this is a matter which still requires attention. The absence of any such relief for losses on capital raised in foreign currencies is a serious anomaly.

In our technical Budget representations for 1979 we outlined proposals that would relieve currency losses and charge currency gains which at present are not within the tax net. We still believe that such a scheme has much to commend it and we therefore repeat our recommendation.

Our proposed scheme would work in the following way. A given date would be selected as the base valuation date for all such borrowings. Exchange profits or losses realised after that date would be taxable or allowable to the extent that the actual repayment liability expressed in sterling differed from the sterling equivalent of the liability at the base valuation date. There would be two saving provisions.

- a The sterling value of the liability when the loan was first taken up by the taxpayer would be used instead of the base date valuation if this produced a smaller taxable gain or a smaller allowable loss.
- b Where the computation showed a profit using the base date valuation, and a loss using the sterling value of the loan when it was first taken up, or vice versa, the realised exchange difference would be neither taxable nor allowable.

In addition, taxpayers would be able to rollover realised exchange gains when one foreign currency borrowing is paid off and replaced by another. Without such a provision, taxpayers could have to liquidate assets to meet a tax liability.

We propose that the base valuation date for our scheme should be 6 April 1979. As before we envisage that exchange profits and losses covered by our proposals would be treated as trading receipts or expenses respectively, and that in the case of investment companies they would be regarded as Schedule D Case VI receipts and management expenses.

GROUP RELIEF FOR CONSORTIUM COMPANIES

Two different aspects of the tax treatment of losses incurred by members of a group of companies are the subject of this representation and the following one. In the long term, we believe that the concept of fiscal consolidation may be the best way of dealing with losses within a group and we shall shortly be setting up a working party to examine this in greater detail. In the meantime, however, we are putting forward these two recommendations for immediate action.

In recent years new technology has become more and more expensive to research, develop and turn to profitable account. Increasingly it requires the combination of several highly complex and advanced skills - skills which may not be found within one business or group of businesses. Firms seeking to exploit this new technology must be able to bring together the necessary finance, resources and expertise and to combine them in one tax efficient business organisation.

The consortium company is one such form of business organisation. From the tax point of view, however, the ability to use losses arising within the consortium company by surrendering them to the owning companies' groups is restricted: only the owning company itself, and not the wider group, may receive a surrender of such losses. Given the substantial group resources that may have to be put into a consortium company, the often slow and expensive lead-in time for projects that are undertaken, and the benefits that may accrue in encouraging companies to combine their skills and to learn from each other, we urge that measures should now be introduced to relax the group relief rules for consortium companies in two ways:

- i tax losses of a consortium company should be available for surrender not only to the consortium members but also to any company in the same group as the consortium member; and
- ii tax losses of companies owning a consortium or in the same group as the owning company should be available for group relief against the profits of the consortium company.

GROUPING OF CAPITAL LOSSES

The group relief provisions in Part XI of the Taxes Act 1970 do not extend to capital losses: a company within a group is regarded as a self-contained unit for capital losses purposes. The Act does not, however, restrict a group's ability to set a gain on one group asset against a loss on another. To achieve this the two assets need only be placed in one company before being disposed of outside the group.

This simple - but in our view unnecessary - expedient may however be time-consuming and it may give rise to practical difficulties. It is therefore nothing more or less than an additional compliance cost to the taxpayer. We strongly recommend that these provisions should be amended so that allowable capital losses may be freely transferred within a group at any time after they have arisen.

SECTION 4

OTHER TECHNICAL REPRESENTATIONS

INTRODUCTION

We come now to our main technical representations. Although we have singled out five recommendations as our 'priority representations' for this year, we nonetheless attach considerable importance to the points outlined below. Our list of technical representations has expanded over the years, as a result of the increasing complexity of our tax legislation, the exacerbating effect of inflation upon many of its defects and anomalies, and the limited time and space which has been available in successive Finance Bills to remedy these matters. In recognition of this last problem we do not repeat all our previous representations on which action has still to be taken; but we have not forgotten them and we reserve the right to return to them in future years if the problems still exist.

Some of our recommendations would necessitate changes in existing practice or current legislation. Others however would only achieve simplification in existing administrative procedures. This does not mean that these latter points have a lower priority. The fact that the right result can be achieved, but only with difficulty, is a powerful argument for remedial legislation rather than a defence of the status quo. This point is particularly true of our fifth priority representation - grouping of capital losses - but it applies equally to other areas.

CORPORATION TAX

Advance Corporation Tax

Many companies are still unable to use their advance corporation tax to full effect because their mainstream corporation tax profits are reduced by, for example, stock relief and capital allowances. A similar problem is the restriction on a company's ability to use its foreign tax credits to the full effect.

These points have been made many times in the past. Nevertheless we have looked at the whole question again; but without altering our earlier conclusion. If these problems are not dealt with the system will continue to tax profits which for tax purposes do not exist. This is clearly inequitable. We therefore urge the Government to make the following changes in the existing rules:

- i It should be possible to set off ACT against the first available corporation tax liability. For example, in the case of a company with a December year end and a tax payment date of 1 January, ACT on dividends paid in June 1979 should be available against tax due on 1 January 1980 rather than 1 January 1981.
- ii The restriction of ACT set-off by reference to the amount of income should be lifted.
- iii The grouping provisions for ACT should be relaxed so that: surplus ACT surrendered to a subsidiary can be carried backwards as well as forwards; ACT can be surrendered in any direction within a group; surrendered ACT is not lost when a company leaves a group as a result of a bona fide commercial transaction; etc.

Group relief - anti-avoidance

Section 29 of the Finance Act 1973 goes much further than necessary to counter wholly artificial group schemes. In order that legitimate transactions would be outside its scope, the following changes should be made:

- The section should specifically include a provision that bona fide transactions will not be penalised. There is no justification for preventing group relief being claimed on the results attributable to the periods of common ownership.
- Where consortia are set up by companies for particular projects, as frequently happens in the construction industry, the terms of agreement often provide that if one of the members wishes to leave a consortium during the project, the consortium members should have first refusal on its share of the enterprise. This is to prevent unwelcome 'outsider' companies from joining the consortium.

The Inland Revenue consider that such an agreement falls within the scope of Section 29, but have indicated that in practice they will not seek to apply it until an offer is made. However, it is unclear both from the wording of the section and from the Revenue statement of practice of 20 October 1973 whether the making of an offer in, say, 1977 in a case where the arrangement was in existence in 1973 would mean the withdrawal of a group relief back to 1973. The position should be clarified without further delay.

The problems caused by this widely drafted legislation have been brought to the Inland Revenue's attention before. We hope that legislation will be introduced at once to limit the scope of the section to cases where tax avoidance is involved.

Definition of control

Under Section 29 (1) (b) (ii) Finance Act 1973, group relief is not available for any accounting period in which a third party could obtain control of either the surrendering company or the claimant company but not both. The definition of "control" is that contained in Section 534 Taxes Act 1970 and, as defined, the common commercial arrangement, where shares in a subsidiary are changed for a loan and the lender is or could become entitled to exercise the votes attaching to the shares, may result in control of the subsidiary passing to the lender.

In such cases, group relief has been denied as a result of this provision in the 1973 Act; but the implications of "control" go far wider than group relief. The lender may often wish to have voting power, or the possibility of obtaining it, as a matter of commercial expediency so he can enforce his security satisfactorily. The definition of control should therefore be amended so as not to encompass this sort of case.

Case V income and charges on income or management expenses

Where a group of companies operates at home and abroad through subsidiaries and loan capital is raised through the holding company, a tax disadvantage can occur. If the holding company's only income is Case V income and it also has charges on income or management expenses, it is required to set them against the Case V income; it may therefore lose the benefit of double taxation relief.

In such cases, to relieve companies of the necessity of rearranging their group structure, they should have the option of carrying forward or grouping charges on income or

management expenses before setting them against the income of the same company. This would bring the treatment of management expenses into line with that of trading losses. Moreover, it is not always possible for a group structure to be rearranged because of other fiscal penalties, such as stamp duty and capital gains tax in certain countries.

Loans and advances on capital account

Section 49 Finance Act 1978 extended the capital gains tax rules so that an irrecoverable loan which has been used by the borrower for the purposes of his trade may count as an allowable loss. This provision will encourage the financing of business undertakings, but it specifically excludes direct loans between companies in the same group.

The normal commercial financing of companies within a group is by way of share capital and loans. If a parent company sells a subsidiary which has been partly financed by share capital and partly by loan, the chargeable gain accruing to the parent will be computed by reference to the share capital after the repayment of the loan. If the disposal realises a loss, no relief is given for the irrecoverable loan. This is inconsistent and unfair, and as a result a large number of companies have taken steps to switch their intra-group loans into either debts on security or into shares. It is unsatisfactory that businesses should have to restructure their financing arrangements simply for this reason.

Moreover, this injustice has been exacerbated by the increasing tendency of the Inland Revenue to invoke the market value rule of Section 22 (4) Finance Act 1965 (now Section 19 (3) Capital Gains Tax Act 1979) on any conversion of a loan into a debt on security or share capital. This follows from the decision in the *Nairn Williamson* case; and we are concerned about it for two reasons. First, companies are being denied relief even though real losses have been incurred. Second, the case gives the Inland Revenue the scope to apply the market value test to commercial share or loan capital subscriptions within groups of companies with the benefit of hindsight.

This position should be changed and we have three recommendations, as follows:

- where companies are members of a group (as defined by Section 272 Taxes Act 1970) non-trading debts between group members should be treated as chargeable assets;
- where a debt is converted into loan stock or shares, the base cost of the new issue should be the amount of the original advance; and
- the base cost of shares or loan stock acquired by subscription should be equal to the amount subscribed, whether the consideration for the issue is cash or the market value of the other assets.

Election time limits

An increasing number of factors may have to be taken into account in determining a corporation tax liability (eg group relief, stock relief, disclaimer of first year allowances, ACT carryback, ACT surrender, Section 177 (2) Taxes Act 1970, double taxation relief). Consequently, it is becoming more and more difficult to ensure that all appropriate claims are made within the two years allowed. This is particularly so in the case of a group of companies, where a contentious point delaying a final tax computation for one member company can have serious repercussions for all the rest. We therefore repeat our recommendation that the various time limits should be increased to six years, as is the case for the surrender of ACT and a claim for double taxation relief.

Interest payable to non-residents

Interest paid to a non-resident may qualify for relief under Sections 248 (4) (b) and 249 Taxes Act 1970 if the borrowing company carries on a trade and the loan was for the purpose of that trade. We believe that two amendments need to be made to Section 249:

- It is common practice in a group for a loan to be raised not by the trading company itself but by a non-trading associated company. Section 249 (3) recognises this to a limited extent by extending relief to a borrowing company which owns 75% or more of the trading company for which the loan is intended. However, no relief is due where - as often happens - the borrowing company is a fellow subsidiary rather than the parent of the trading company. This is inequitable and we therefore recommend that the rule in Section 249 (3) should be extended so that a borrowing company may qualify for interest relief on a loan taken out on behalf of another company, provided that both are 75% subsidiaries of the third company.
- Section 249 (2) denies relief for interest paid to a non-resident company where either the borrower or the lender controls the other, or where both are controlled by a third company. This restriction is unnecessarily severe and could penalise bona fide commercial loans. The other conditions for relief are sufficiently stringent to guard against abuse, even where payments are between associated companies. This additional restriction imposed by Section 249 (2) should therefore be removed.

Close companies: apportionment

Paragraph 5 (6) (a) Schedule 16 Finance Act 1972, is unnecessarily restrictive and should be abolished. It should be sufficient to prove that there has been a subsequent over-distribution; it should no longer be necessary to identify the subsequent dividend with specific profits earned previously.

INCOME TAX

Provision for retirement: (i) retirement annuity reliefs

Successive Governments have attempted through the tax system to encourage employers, employees and the self-employed to make adequate financial provision for retirement and for dependants. We have always supported such objectives. However, despite recent developments in the tax provisions, the benefits available to the self-employed through approved retirement annuity policies are much less advantageous compared with the benefits available to employees and even to director-proprietors of small firms.

It is entirely illogical that the pension benefit of a self-employed person should be determined by reference to the limited annual contribution that ranks for tax relief, while the employee's pension is generally a factor of final remuneration. Moreover, in the early years of a business the income of a self-employed person may be very low while he is developing his trade: any surplus funds will probably be used to finance the business rather than to pay pension contributions. The self-employed should therefore be able to top up their pension contributions in later years, when their businesses are thriving.

The importance of the self-employed to the economy is now widely accepted. It is iniquitous that they should be penalised in this way.

We therefore propose that:

- the annual fixed limit of £3,000 should be abolished;
- the present 15% earnings limit should be brought into line with the annual cost of funding a full two-thirds pension under an occupational pension scheme;
- where maximum allowable contributions have not been made in past years, it should be possible to carry forward the shortfall and pay it in subsequent years with a full tax relief; and
- on retirement or ceasing to be engaged in the business, the self-employed person should be permitted to top up his pension by paying the premium required to cover a full two-thirds pension on the average of his best three years earnings. Tax relief on this additional premium should be spread back over his last six years in business.

Provision for retirement: (ii) partnership annuities

The amount of any annuity paid under the terms of a partnership deed which is treated as earned income under Section 16 Finance Act 1974 should be adjusted for inflation. The present limit of 50% of the former partner's average earnings in the best three years of his last seven years becomes less realistic as time passes.

DEVELOPMENT LAND TAX

(Statutory references are to the Development Land Act 1976.)

Deferment of DLT on development for own use

Section 19 of the Act permits a liability to development land tax arising on a deemed disposal to be deferred where the land or building is to be used for the industrial purposes of the chargeable person's trade. This section however only applies to buildings within the scope of Class E in Paragraph 7, Schedule 4 of the Act.

The present rules are unsatisfactory for two reasons:

- Some buildings are excluded for no apparent logical reason. Thus, a warehouse only appears to qualify if it is built within the same curtilage as a factory which utilises its storage space. Even with the recent reduction in the DLT rate, this still provides an overwhelming financial incentive to build a warehouse next to a relevant factory even if proper commercial analysis indicates that it should be built elsewhere. This cannot be good for the nation's industry.
- All buildings used by non-industrial businesses are excluded. This is inequitable: these buildings are valuable to the economy in that they provide essential services to industrial concerns and generate export earnings in their own right.

The CBI recommends that the definition in Section 19 should be widened to include all buildings which are to be used by the chargeable person in his business.

Extension and demolition and rebuilding

In order to facilitate reorganisation of industrial sites in the most efficient and logical way, we propose two amendments to Schedule 4 of the Act:

- Paragraph 5 (1) (a) of the Schedule should be amended so that an extension to one or more of a number of buildings within the curtilage of an industrial site should not constitute material development if, taken together, the cubic content of all the buildings within that curtilage is not increased by more than 10%.
- Paragraph 5 (a) (b) of the Schedule should be amended to include the demolition and rebuilding of a building on a different part of the same industrial site, provided that the cubic capacity of the new building does not exceed 110% of the aggregate cubic capacity of the demolished building and others in the same curtilage. The present Inland Revenue interpretation of the term 'rebuilding' seems to require rebuilding to be carried out on the precise spot occupied by the original building unless the enlargement is part of a development scheme affecting other buildings.

Exemption for development within three years of acquisition

Requests for exemption under Section 18 of the Act (exemption for projects begun within three years of acquisition of land) are proving to be a time consuming and expensive exercise. This is a contradiction of the basic intention of the section which was to simplify matters where land has been acquired at a full price for immediate development. The main difficulty arises from the insistence of the DLT Office upon a complete outline of the scheme in order to assess whether the site was purchased at a price which included the full development value inherent in the scheme.

Rollover relief on surrender and re-grant of a lease

A form of rollover relief is provided under Section 44(4) and paragraph 17 Schedule 2 of the Act where there is a material variation in the terms and conditions of a lease. The same provisions should apply where a lease is surrendered in return for the grant of a new lease on the same property.

Payment of DLT and interest on late payments

The system of notifying and collecting tax on deemed disposals has a logical structure; notification must be given within 30 days of the deemed disposal and then, if the taxpayer so elects, the tax becomes payable by instalments starting twelve months after the deemed disposal. Interest is only charged on late payments. On the other hand, there is no discernible logic in the arrangements which apply for real disposals, requiring notification to be made within one year of the disposal. Tax becomes payable three months after the disposal or 30 days after the issue of the assessment, whichever is the later, but interest is charged on any tax still unpaid three months after the disposal.

It is wrong that the charge to interest should be entirely divorced from the notification procedure so that it may well apply before the due date for payment. The system should be restructured as follows: a notification of a real disposal should be made within, say, six months of the disposal; the due date for payment should be nine months after the disposal or 30 days after the assessment, whichever is the later; and interest should be charged on one of two bases:

- where notification has been made within six months from the disposal date, interest should run from the due and payable date; and
- where notification has not been made within the six months period, interest should run from nine months after the disposal date.

Such a system would be fairer to the taxpayer and to the Revenue. The interest charge would encourage the taxpayer to notify disposals to the Revenue in good time and the taxpayer would be protected from an interest charge where he had notified the Revenue in accordance with the rules and for some reason an assessment was raised late.

Approved pension schemes

Approved pension schemes should be treated for all tax purposes at least as favourably as charities: they should therefore be exempt from DLT in respect of any disposal of an interest in land held on or before 12 September 1974.

VALUE ADDED TAX

With the increase in VAT to 15% it is all the more important that registered persons should not have to account for VAT on bad debts. The limited relief introduced in the Finance Act of 1978 only applies to cases where the customer has been made bankrupt or has gone into liquidation. In many cases it will not be worthwhile for a supplier to go so far as this to pursue his debt and no other person may take the necessary action.

We therefore recommend that the relief should be extended so that the rules are the same as those which apply for income tax and corporation tax purposes. On any subsequent payment of the debt in whole or in part the supplier would then be liable to account for an appropriate amount of VAT.

MISCELLANEOUS

Construction industry - tax deduction scheme

The Inland Revenue have recently issued a consultative document on this subject and we shall be offering detailed comments in due course. In the meantime, however, we repeat our representation submitted in 1979 that firms not primarily involved in construction may nevertheless find themselves classed as 'contractors' under Section 69 (3) Finance (No 2) Act 1975 even though their 'construction operations' extend only to necessary repairs, maintenance and construction work connected with their own trades. This is an unnecessary administrative burden and we recommend that such firms should be excluded from the scheme.

Costs of tax appeals

The decision of a taxpayer whether or not to appeal against a tax assessment is made even more difficult by the consideration that if his appeal fails he will have to bear a substantial proportion of the costs. This is particularly so where the amount of tax involved is small, however good his case may be.

We therefore recommend that if, at any stage in the determination of a particular issue, the taxpayer succeeds and the Revenue appeal to a higher authority, the taxpayer's costs should be borne by the Revenue whether or not their appeal succeeds.

Capital allowances in the mining industry

In past years we have recommended that mining capital allowances be simplified and brought into line with other capital allowances where the emphasis is on incentives for industry. A joint working party set up by the representative bodies involved has submitted separate representations, which we fully support. Like the working party we believe that all capital expenditure in the mining industry, which is not otherwise relieved, should qualify for mining allowances and be dealt with under a 'pool' system, similar to that for plant and machinery.

PERSONAL & CONFIDENTIAL



H M Treasury

Parliament Street London SW1P 3AG

J B Unwin

Under Secretary

Switchboard 01-233 3000

Direct Dialling 01-233 3016

1980
p.a. (Budget
file)

B.

8 February 1980

T P Lankester Esq
10 Downing Street
LONDON SW1

1872

Dear Sir,

TIMETABLE FOR MAIN DECISIONS ON THE BUDGET ETC

As promised, I enclose a copy of our "master" timetable for the Budget and related matters. This will give you an idea of how we see the various decisions moving forward, including the possible financial plan we had a brief word about.

2. This is in a sense an ideal timetable and the facts of life will no doubt ensure that there are slippages. But there is not much room for slippage if we are to avoid severe pressure at the later stages.

3. I should welcome a further word with you on the question of consultation with the Prime Minister. My own advice to the Chancellor has been that he ought to aim to open up with the Prime Minister as early as possible during the week beginning Monday 18 February. There is also the question of the Budget Cabinet. Ecclesiastical pre-occupations may rule out 25 March; but for a variety of reasons the Prime Minister may not, I suppose, want to hold it any earlier. However, if it is to be held (like last June) on Budget morning itself, we should have to be pretty certain that the risk of changes was negligible.

4. Perhaps we could arrange a word when you have had a change to look at this. I should, of course, be very grateful if you would regard it as for your personal information only.

J B Unwin

J B UNWIN

PERSONAL & CONFIDENTIAL

MR UNWIN or ←

cc Principal Private
Secretary (personal)
Sir Douglas Wass
Mr Burns
Sir Kenneth Couzens
Sir Anthony Kawlinson
Mr Ryrle
Mr Byatt
Mr F Jones
Mr Littler
Mr Middleton
Mr Battishill
Mr Bridgeman
Mr Britton
Miss Brown
Mr F E R Butler
Mr Cassell
Mr Shepherd
Mr Bottrill
Mr Collinson
Mr P Davies
Mr Neuburger
Mr Riley
Mr Sedgwick
Mr Lay
Mr Melliss
Mr Mortimer
Mr Kingsley)
Mr Sabel) ORU
Mr MacAuslan

PS/Customs
PS/Inland Revenue
Mr Ridley

TIMETABLE FOR MAIN DECISIONS ON THE BUDGET AND RELATED EXERCISES

1. I have put separately to you today a copy of the Budget and MTFP timetable for submission to the Chancellor. That is a condensed version, shorn of details about FPC and PCC meetings etc, of the fuller timetable attached to this note which reflects the outcome of some regrettably prolonged discussions within the Treasury and with the revenue Departments.
2. I circulate this fuller version as a guide to the preparation of more detailed schedules for particular purposes (for example, a schedule for the pre-Budget weekend through to delivery of the speech is I think customarily circulated by the Chancellor's Office, and Accounts prepare a fully detailed FSBR timetable).
3. There are a few points I should record in addition to those made in the covering note to the Chancellor's version:

i. some of the wording of the various timetable entries on the MTFP and the £M3 roll-over assumes that monetary targets will continue to be expressed as growth rates. But this is of course without prejudice to the possibility of adopting targets for the money stock instead - as canvassed in Mr Cassell's 1 February minute to Sir Douglas Wass on a medium-term plan or framework.

ii. the timetable for preparation of post-Budget medium-term revenue projections, involving the Revenue as well as MP, is based on the assumption that there would be only a "single case" for such medium term projections in the FSBR. This is consistent with the approach to an MTFP outlined in Mr Cassell's minute and attachment. If in the event we were obliged to prepare more than one case then the timetable would have to be reviewed with the aim of giving the Revenue as much extra time as possible between circulation of a draft post-Budget forecast and the deadline for preparation of tax revenue projections.

iii. the printing schedule for the FSBR assumes that we will have to produce a 48 page FSBR. This means that the Part I Review of the past year will have to be got to the printer by 19 March to allow composing of an 8 page section before the pre-Budget weekend. An FSBR of between 48 and 56 pages seems unlikely but if it were to prove necessary some other FSBR sections would also have to be got to the printers before 21 March. Accounts and CU will be keeping an eye on this possibility.

M T Folger
M T FOLGER

4 February 1980

CONFIDENTIAL

date	11 February	12	13	14	15
Budget { decisions speech etc				2) PCC discussion of forecast & Budget judgment.	advice to the Chancellor on the Budget judgment
MTFP and/or medium-term material for the FSBR					definitive advice to the Chancellor, on (a) the form of a MTFP (b) the £M3 growth targets 1980-81 to 1981-2
FSBR { Prospects = Parts II = III Review					
Forecasts			NIF Short Report to PCC and Revenue Departments		NIF Short Report to Treasury Ministers
Budget Briefing					
Contacts outside the Treasury, etc					
PEWP 2					draft White Paper submitted to Treasury Ministers

CONFIDENTIAL

date	18 February	19	20	21	22	
Budget { decisions speech etc	decide final range of VEB options [possible meeting of FPC to discuss implications of the forecast and the Budget judgment for tax measures]				provisional decisions on (a) £ M3 roll-forward for 1980-81 and (b) PSBR for that year (see also MTFP entry)	
MTFP and/or medium-term material for the FSBR					1) Final decisions on form of a MTFP 2) Provisional decisions on £ M3 growth rates to 1983-84	
FSBR { Prospects - Parts II - III Review						
Forecasts						
Budget Briefing						
Contacts outside the Treasury, etc						
EWP 2				proof to printer incorporating Treasury Ministers' amendments		

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	date	25 February	26	27	28	29	
Budget	decisions					a) final decisions on Customs structural changes b) decide limited range of Customs rate changes	
	speech etc	a) draft outline to Chance for b) CU commissions contributions from divisions				divisions' contributions to CU	
	MTEP and/or medium-term material for the FSBR			[interim report to Ministers as necessary eg if provisional \pm M3 decisions seem untenable]			
FSBR	Prospects + Parts II + III						
	Review			draft circulated to under-secretaries by EB			
	Forecasts						
	Budget Briefing			contributions for pre-Budget brief to EB			
	Contacts outside the Treasury, etc			any macroeconomic paper for 5 March NEBC to be circulated to Com.:			
	P/EWP 2		proofs circulated to Cabinet for clearance				

CONFIDENTIAL

date	3 March	4	5	6	7
Budget	decisions	target date for provisional revenue decisions	deadline for provisional revenue decisions to forecasters	deadline for provisional revenue decisions to forecasters	a) Final decisions on Customs taxes and main Revenue taxes (incl. capital taxes) b) Final VEB decision
	speech etc				draft speech circulated to PCC
MTEP and/or medium-term material for the FSBR		submit to Chancellor 1 st draft of MTEP and/or medium-term FSBR material			submit to Chancellor 2 nd draft of MTEP and/or medium-term FSBR material
FSBR	Prospects * Parts II * III				
	Review	draft to Chancellor and CEA		Chancellor and CEA's comments to EB	
Forecasts				first draft of the post-Budget forecast circulated within Treasury and to Revenue Departments	final pre-Budget "update" circulated.
Budget Briefing			a) pre-Budget brief circulated b) DEB commissions contributing to main Budget brief.		
Contacts outside the Treasury, etc	[Chancellor to discuss shape of Budget decisions with the Prime Minister]		macroeconomic discussion in NUBC		
PEWP 2	deadline for Cabinet clearance of profits				

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	10 March	11	12	13	14
date	10 March	11	12	13	14
Budget { decisions			final decision on NIS rates for end August implementation	[meeting with Secretary of State on cost amounts of social security updating]	
Budget { speech etc		PCC to discuss draft speech		full draft submitted to Chancellor	
MTFP and/or medium-term material for the FSBR	(preliminary information on February EM3 becomes available)		final confirmation of £ M3 roll-over for 1980-81		
FSBR { Prospects " Parts II & III			submit complete draft to Chancellor covering MTFP/medium term material (as revised), Industry Act forecast, provisional forecasts of public sector transactions		submit revised complete drafts to Chancellor taking account of post-Budget forecast and Ministerial comments on 12 March 1980
	Review	version for printing sent to Accounts by EB			
Forecasts			Revenue Departments provide provisional post-Budget revenue forecasts		
			[successive revisions of the post-Budget forecast] ----->		
Budget Briefing					noon deadline for contributions to main Budget brief
Contracts outside the Treasury, etc					
PEWP 2					

CONFIDENTIAL

date	17 March	18	19	20	21	
Budget {	decisions on minor Revenue issues		/	/		
	speech etc	2 nd full draft speech to Chancellor (1) draft text of Budget broadcast to Chancellor			target date for finalising broadcast text	
MTEP and/or medium-term material for the FSBR	/	/	/	/	/	
FSBR {	Prospects = Parts II & III	final draft to Chancellor reflecting comments on 14 March version and other tidying-up.	version for printing to be with Accounts		proofs returned by printers	finally corrected proofs to be with Accounts, by noon, for composing.
	Review		finally corrected proofs to be with Accounts, by noon, for printing	/	/	/
Forecasts	Revenue Departments provide final revenue forecasts.					
Budget Briefing						
Contacts outside the Treasury, etc						
PEWP 2		White Paper published	/			

CONFIDENTIAL

date	24 March	25	26	27	28
Budget {	decisions	/	/		
	speech etc			delivered in the House	
MTFP and/or medium-term material for the FSBR	/	/	/		
FSBR {	Prospects * Parts II & III		printing commences early afternoon	} published	
	Review	/	/		
Forecasts					
Budget Briefing			finalise briefs in light of Budget Cabinet reproduce copies		
Contacts outside the Treasury, etc			Budget Cabinet (contingent on Entitlement complication)		
PEWP 2	/	/	/		

cc Euro Pol Pt 3
European Council Mtg.

Chambers
Told Cabinet staff 14/2 26 March
I have discussed with Michael.

Germany Pt 2
Chancellor Schmidt's visits to UK.

CLIVE

her us begin. Cabinet at 0930.
Do that 1100 start for the briefing meeting based on
a 0930 Cabinet or a 1000 Cabinet? If this letter, can
we not begin the briefing meeting at 1030 or at 1045?

Budget Cabinet/Briefing for Schmidt and

European Council

MLH
7:1

You asked me to have a further word with Nick about the necessity of the Prime Minister sitting in on the second day of the Budget Debate, i.e., Thursday, 27 March. Nick is quite clear that she should, if possible, do so as there will be some major speeches being made, mostly on the Opposition side.

D. Healey
kicks off
with the

Opp's considered views MJS

Robert Armstrong has come up with the following suggestion: that the Budget Cabinet takes place on Wednesday, 26 March (Budget Day) at 10.00 a.m. or even 9.30(?) and that the European Council briefing meeting should start at 1100 and run through to 1300 hours. There would be a normal Cabinet starting at 1030 on Thursday 27th.

Could I have your views on this suggestion, please?

ES.

7 February 1980

Econ P3l



10 DOWNING STREET

T.P.

See Ch/Ex to PM 24.7.79
(at Hay)

Tolkien, HMT, says Inland Revenue
working on this as part of an
overall review of corporation tax.

Lord Cockfield will be making
recommendations to Chancellor
and thence to P.M. Lengthy

business, HMT will be in touch
when have something to report.

? Remove from B.F. for time
being.

Steve

Yes, Ms.

31. 1. 80.
rumor from (BP) - T.

Original in
Church file

26 January 1980

My dear Bishop,

Thank you for your letter of 24 January about your Enthronement on 25 March. You will know how glad I am that we have been able to change the Budget date, and I am deeply grateful to you for the spirit in which you have spoken about this.

Mr Callaghan and I have been in touch about Question Time on 25 March, and I am delighted to say that there is now nothing to prevent me coming to Canterbury. You know how much I shall look forward to being with you.

Yours sincerely,

MARGARET THATCHER

The Right Reverend
The Lord Bishop of St Albans

TTC



*Original
clipping*

10 DOWNING STREET

THE PRIME MINISTER

24 January 1980

Dear Cardinal Hume.

Thank you for your letter of 21 January about Budget Day and the new Archbishop of Canterbury's Enthronement.

I am very glad that it has proved possible to change the date of the Budget to Wednesday 26 March.

*Yours sincerely
Margaret Thatcher*

His Eminence
The Cardinal Archbishop of Westminster



Original
in Church of England

10 DOWNING STREET

THE PRIME MINISTER

24 January 1980

My dear Lord Bishop.

Thank you for your letter of 21 January about Budget Day and the new Archbishop of Canterbury's Enthronement.

I am very glad that it has proved possible to change the date of the Budget to Wednesday 26 March, and I hope you will be pleased.

Yours sincerely
Margaret Thatcher

The Right Reverend
The Lord Bishop of London



Original in
Church filing

10 DOWNING STREET

THE PRIME MINISTER

24 January 1980

My dear Archbishop.

Thank you for your letter of 21 January 1980 about Budget Day and the new Archbishop of Canterbury's Enthronement.

I am so sorry for any distress that has been caused and I am glad that it has proved possible to change the date of the Budget to Wednesday, 26 March.

Yours sincerely
Margaret Thatcher

His Grace The Lord Archbishop of Canterbury

The Times 23 January 1980

Budget changed to March 26 to avoid clash

By Fred Emery
Political Editor

The Government relented yesterday, decided to serve Mammón last, and switched Budget day to Wednesday, March 26, so as not to clash with the March 25 enthronement of the Archbishop of Canterbury.

The Government's postponement was greeted in the Commons with relief by members of all parties, but not before a Conservative backbencher had asked why the parties could not have referred to their diaries before confirming dates of important national events.

The fault for the blunder lies entirely with ministers since they knew weeks before-

hand of the Canterbury Cathedral ceremony before deciding to have the Budget on the same day.

Protests from churchmen at such insensitivity were supported by cries of consternation from Conservatives that their party should have shown such ineptitude.

Mr Norman St John Stevas, Chancellor of the Duchy of Lancaster and Leader of the House, the Government's leading Roman Catholic, attempted to put the best face on the Government's about-face.

It gave him great pleasure to "reconcile Canterbury and Westminster", he said, although Mr Michael Foot, for the Labour Opposition, ironically

welcomed what he called a "minor U-turn".

In his letter to the Archbishop designate, the Right Rev Robert Runcie, Bishop of St Albans, Sir Geoffrey Howe, QC, the Chancellor of the Exchequer, did not manage an apology so much as a laboured explanation of why it now proved possible to move the Budget.

The upshot seemed that although the week of March 22 was imperative for the Budget, Tuesday had been chosen in the first place because, he said, "there are good practical reasons for the well established convention that Budget Day should be a Tuesday".

Ian Bradley writes: The Very

Rev Victor de Waal, Dean of Canterbury, said last night that he welcomed the Government's flexibility.

He said he hoped it would mean that all three major party leaders would attend the enthronement as they did Dr Coggan's enthronement in 1975.

A spokesman for the cathedral said that definite acceptances had been received from Sir Keith Joseph, Sir Ian Gilmour, Lord Carrington, Mr Michael Heseltine, and Mr David Steel.

He said the cathedral was particularly pleased that Mr William Whitelaw would be able to attend the enthronement because he was a personal friend of Bishop Runcie.

Business News Diary, page 21

Econ Pol

PRIME MINISTER

Meeting with the Chancellor

I imagine you will want to go over the public expenditure paper for Cabinet - including any further thoughts from the Chancellor on social security. I enclose in this folder the material which I gave you for this evening's meeting with him and Mr. Jenkin. One point which I have established is that the ERS could be abolished with effect from 1982 without any criticism that we were breaking the "contribution contract". ERS contributions in Year 1 are assumed to pay for ERS benefits in Years 2 and 3 - i.e., it is not a funded scheme like a pension.

I have mentioned to the Treasury that you are very doubtful about the Chancellor's capital taxation proposals - simply because we won't have the money to pay for them. They tell me that the Chancellor is also having second thoughts, and will almost certainly want to cut it down in size and scope. In any case, final decisions on the package are not needed for quite a while.

I also enclose Len Murray's letter to the Chancellor asking for a meeting to discuss steel and coal.

R.

23 January, 1980.

12 DOWNING STREET,
S.W.1.

With

Vms

The Private Secretary's

Compliments

Econ B/L

BUSINESS STATEMENT

TUESDAY, 22nd JANUARY, 1980

LEADER OF THE HOUSE

With permission, Mr Speaker, I should like to inform the House that my Rt Hon and Learned Friend, the Chancellor of the Exchequer, now proposes to open his Budget on Wednesday 26th March 1980, and not on Tuesday 25th March as previously announced.

I am sure that this change will be welcome to Rt Hon and hon Members on all sides of the House.

44 JAN 1980



1980





2
Pm
The Chancellor
will be writing

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

18 January, 1980

Mr Peterson

My dear Bob,

I thought I should write to you today to let you know why I am having to present my Budget on the day of your enthronement, and to assure you - not that I suppose for a moment that you would think otherwise - that I am not engaged in a dark conspiracy to distract attention from the Canterbury installation. I should have liked nothing better than to witness your great day.

The problem, which I imagine you understand very well already, is that a Chancellor has in practice very little room for manoeuvre in his choice of Budget Day. The sheer mechanics of the operation - the physical production of the speech, final consultations with colleagues and so on - make Tuesday very much the best day, as successive Chancellors have found.

But even if Tuesday is based on much more than tradition, why pick on your Tuesday? Ironically enough my choice has been very much influenced by the dictates of the ecclesiastical calendar. We need to set the Budget date as close as possible to the end of March; delays could mean lost revenue, while advancing the date means that we are without important information about the year just gone. With the Tuesday before Easter, and the two succeeding Tuesdays more or less ruled out, 25th March was in effect our only option.

The problem does become a little easier in years when Easter is late. My impression is that Easter in the Orthodox Church is never earlier than in Western Christendom,

/and that

The Rt. Rev. The Lord Bishop of St. Albans, MC., MA



and that quite often it is two weeks later. So perhaps I and my successors can look for some help from your discussions with your Orthodox counterparts!

Will come good with

As ~

Howe

(GEOFFREY HOWE)

PRIME MINISTER

Lambeth Palace have told me that there is some unhappiness in the Church, apparently very much shared by the Free Churches, that Budget Day and Bishop Runcie's Enthronement at Canterbury coincide on 25 March. People are quicker than they should be to feel that this is something of a slight by the Government to Bishop Runcie. There is also the problem of TV coverage for both events - the Enthronement is at 3 pm - and some churchmen clearly feel that the Budget will distract attention generally from the Enthronement.

In fact, both dates will have more or less dictated themselves, the Enthronement because March 25th is a great Feast (the Annunciation) and the Budget because it has to be a Tuesday and because of the date of Easter this year.

I understand that the Chancellor of the Exchequer has written to Bishop Runcie to say how sorry he is that the dates coincide, and explaining why the Budget had to be fixed for 25 March.

It is unfortunate, but I hope that things will calm down.

CVP

18 January 1980

I also am very unhappy - is it possible to change the date of the enthronement? Even if the Budget had been the 24th - we should still have had to be in the House on the 25th because of the opening of the Opposition case.
mb.

The Times
18 January 1980.

Budget on day of Primate's enthronement

By Our Political Editor

Budget day is to be Tuesday, March 25, the day the new Archbishop of Canterbury is enthroned, it was announced in the Commons yesterday. Indicating that he would prefer to attend the enthronement, Mr Norman St John-Stevas, Leader of the House, gave no reasons for the clash of dates.

It was said later by ministers that since the Government intended to have fewer budgets than its predecessor, it was easier for Sir Geoffrey Howe, QC, Chancellor of the Exchequer, to announce the date well in advance, an interpretation hardly calculated to impress the new Archbishop.

EEC decision, page 17

CONFIDENTIAL

Prime Minister

Econ PA

Agree ?



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

PL

14th January, 1980

14/1

PA

Spoke to PM/told Chief Whips office, CDE and TEG that date was to be announced tomorrow 15/1

Dear Tyn,

ANNOUNCEMENT OF THE DATE OF THE BUDGET

As you will be aware, the Prime Minister has agreed to the Chancellor's proposal that the date of the Budget should be Tuesday, 25th March. As you know, the Prime Minister and the Chancellor last Thursday had a brief discussion about the best date for announcing this, in light of the fact that it coincides with the date of installation of the new Archbishop of Canterbury.

The Chancellor has now considered this further and has concluded that there is no good reason for holding back on an announcement. In these circumstances the Chancellor feels that it would be sensible for him to tell Cabinet about the date of the Budget next Thursday, 17th January, and have an announcement in Parliament that afternoon.

The usual method for making the announcement in Parliament is for the Leader of the House to give the information in reply to a question by the Leader of the Opposition (prompted by the Chief Whip) on the Thursday Business Statement. It would seem sensible to follow this course next Thursday.

I am copying this letter to John Stevens and Murdo Maclean.

yours ever

John Wiggins

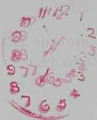
(A.J. WIGGINS)

T.P. Lankester, Esq.,
Private Secretary,
10, Downing Street

CONFIDENTIAL

Why can't it be announced without promulgating?

14 JAN 1969



- ① Supp's Recs app
- ② Comp
- ③ Affairs
- ④ Deten

CONFIDENTIALEcon Pad

4 January 1980

Capital Taxation

I am sorry that the Chancellor of the Exchequer has not had an earlier response to his minute of 12 December 1979 to the Prime Minister about his review of capital taxation.

The Prime Minister has read the minute and has commented that it is a very good paper. She has asked me to say that she agrees with the elements of the package summarised in paragraph 16 of the minute and is content for the Chancellor of the Exchequer to go ahead with planning and the drafting of legislation on that basis. She does not see any need for a meeting at this stage.

C. A. WHITMORE

A. M. W. Battishill, Esq.,
H.M. Treasury.

CONFIDENTIAL



Top copy in National Health
Oct 1979
Nurses Pay. Clegg Commission
Kept

10 DOWNING STREET

From the Principal Private Secretary

3 January 1980

Dear Tony,

When the Prime Minister saw the Chancellor of the Exchequer at 1430 this afternoon they discussed the following subjects.

Appointments at the Bank of England

The Prime Minister said that she had given careful consideration to the Chancellor of the Exchequer's minute of 31 December, 1979. She had told the Governor in December that she agreed very reluctantly to the proposal to appoint Mr. McMahon to be Deputy Governor in succession to Sir Jasper Hollom, but since then she had seen much more of the individuals concerned in connection with the question of Iranian assets. In that context Sir Jasper Hollom had stood head and shoulders above all the other representatives of the Bank, including Mr. McMahon. He had shown himself to be both steady and decisive in a difficult situation. She had been surprised to learn that he was only 62, and she did not believe that we could afford to let him go. She would much prefer that rather than appoint Mr. McMahon, Sir Jasper Hollom should continue as Deputy Governor.

The Chancellor of the Exchequer said that, following his talk with the Prime Minister, the Governor was now planning a number of staff appointments on the assumption that Mr. McMahon would become Deputy Governor, and it was likely that it would cause considerable difficulty if the earlier decision that Mr. McMahon should succeed Sir Jasper Hollom was now reversed. Personally, he thought better of Mr. McMahon than did the Prime Minister. Nonetheless, he would now see the Governor to let him know that the Prime Minister wished Sir Jasper Hollom to be kept on. It might be necessary for the Prime Minister to see Mr. Richardson herself. The Prime Minister said that she was very ready to do this.

Clegg: Nurses' Pay

The Prime Minister and the Chancellor of the Exchequer agreed that the Press announcement about the Clegg award on nurses' pay should not contain any mention of increasing cash limits in order to accommodate the cost of the pay award, lest this should have repercussions on the present steel dispute. They agreed the lines of a form of words to be used, and we in this office are now pursuing the matter in separate correspondence.

/Date of the Budget

Date of the Budget

The Chancellor of the Exchequer said that he wished to confirm that 25 March was still acceptable to the Prime Minister as the date for the Budget. The Prime Minister said that it was.

Senior Appointments in the Treasury

I have recorded the discussion on this subject in a separate letter to you.

Yours ever,

Alvin White.

A.M.W. Battishill, Esq.

SENIOR STAFF IN CONFIDENCE

Original on Bristol ^{Form 101} # 4
Future Policy towards EEC
Community Budget.

cc Mr Whitmore

NOTE FOR THE RECORD

The Chancellor of the Exchequer called on the Prime Minister at 0845 hours today. The following are the main points which came up in discussion:

(i) EEC Budget

The Chancellor said that the Lord Privy Seal was establishing a small official group to assist him in developing our negotiating strategy on the EEC Budget issue. Four FCO officials were to be on this group, but only one Treasury official had been invited. While accepting that the FCO had to be in the lead, he felt that the Treasury had a crucial role to play; and therefore Treasury representation on the group should be on a par with the FCO. The Prime Minister agreed that Treasury representation should be stronger, and that - in addition to Sir Ken Couzens - there should be at least two other Treasury representatives. (We have since spoken to Sir Ian Gilmour's Office about this, and he is taking the necessary action.)

(ii) Treasury Appointments

The Chancellor asked the Prime Minister whether she had been able to form a view of Mr. Ryrie when she visited Washington. The Prime Minister replied that she had not been very impressed by him: in particular, she had not found his manner at all easy, and this suggested to her that he would not be very good at managing a major part of the Department. The Chancellor said that he was also having doubts about Mr. Ryrie's succeeding Sir Lawrence Airey. But he had not yet taken a final view, and would come back to the Prime Minister in the New Year.

(iii) Budget Date

The Chancellor said there were two options: either 25 March or 22 April. His own provisional preference was for 25 March mainly because the later date would involve

a loss of about £100 million (assuming the indirect taxes were revalorized). After the late Budget this year, he also did not want a repeat. The Prime Minister said that she agreed.

(iv) Monetary Policy

The Chancellor said that the Treasury were reviewing various aspects of monetary policy, including the Bank's performance in October and also the proposals for Monetary Base Control. He would be letting the Prime Minister have a note fairly soon. Moreover, he had promised a paper on monetary policy to Cabinet.

R.

Orig. Defence May 79
Budget.

SECRET

From P. J. 6

PRIME MINISTER

MEETING WITH THE CHANCELLOR: THURSDAY 13 DECEMBER

The following issues are likely to be raised by the Chancellor:

(i) Public Expenditure

There is the note he sent you about defence expenditure (Flag A) on which Robert Armstrong commented at length. You will presumably want to persuade the Chancellor not to make a pitch in Cabinet against the defence spending volume figures. We are likely to have enough trouble getting Mr. Pym to agree the cash limits. There is also a note which came today (Flag B) on the other main options for spending cuts.

(Robert Armstrong's note on handling of bilateral
on 'star chamber' is at Flag F).

(ii) Capital Taxation

There is a minute at Flag C in which the Chancellor sets out his provisional proposals - these involve abolishing the investment income surcharge altogether, and significantly reducing the burden of capital gains tax and capital transfer tax. You won't have time to discuss this in detail tomorrow. You might prefer to set up a meeting with one or two other Ministers - for example Mr. Nott and Sir Keith Joseph because of their interest in the industrial implications, and perhaps the Home Secretary to provide a political steer. The main issue will be whether the Chancellor can afford the whole package which will cost about £600 million. In the light of this afternoon's discussion on small firms, it might for example be better to spend rather less on CPT and spend £50 million on the small firms "start up" scheme.

(iii) Treasury Appointments

A meeting has been arranged for Friday morning with Ian Bancroft and others to discuss this, but the Chancellor wants a preliminary word. (Ian Bancroft's note at Flag E).

/Following your

Following your meetings today about the Local Government Bill, you may want to mention to the Chancellor the capital controls issue. Mr. Heseltine told you that his full package would be saleable, but that the aspects which the local authorities most wanted could not be announced until he and the Treasury (Mr. Lawson) had come to terms over the new arrangements to replace project controls. You told Mr. Heseltine that you would send a message to Mr. Lawson urging the fastest possible progress on this. In practice it might be best to do this by asking the Chancellor to see that work is expedited.

At E this afternoon, it was decided that the Chancellor should look again at the small firms "start up" scheme. But I think there was no suggestion that there should be any announcement before the Budget. I wonder whether the Chancellor should not be pressed to have something ready for an announcement earlier than the Budget. Although implementation would have to await the Finance Bill, this might bring forward decisions by potential investors. And it would be politically helpful. (We did write to the Treasury last month suggesting that an announcement before the Budget would be helpful - see Flag D.)

R

12 December 1979

900

BF

More summary
of memo 16!
not

SECRET



Prime Minister

S 4

The Chancellor will want to
talk this with you tomorrow.
The main question in my mind
is whether we can afford the
package - and whether
other things (such as the

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

PRIME MINISTER

£50 on the small firms (start-
up) might not be better

T.
12/12

Not
Does good
paper
not.

from
Tamm
T.
17/12

CAPITAL TAXATION

I don't think you have
a chance to read this -
you can

My colleagues and I have been making a very thorough
review of the Capital Tax situation and I should be glad of an
opportunity to discuss with you our provisional conclusions. *distance*
America.

2. In the General Election Manifesto we said:-

T
13/12

"We reject Labour's plans for a Wealth Tax.
We shall deal with the most damaging features
of the Capital Transfer Tax and Capital Gains
Taxes, and propose a simpler and less
oppressive system of capital taxation in the
longer term." (page 14)

3. We made a start in the June Budget: we raised the threshold
for the investment income surcharge (IIS) and made reductions in
development land tax. However capital transfer tax (CTT) and
capital gains tax (CGT) raised issues that were too complex to
be dealt with in the time available. In my Budget Speech I said:-

"I have, therefore, decided that we should not
attempt to deal with them in the coming Finance
Bill - abbreviated as it is bound to be - but
should press ahead with a thorough study, with
a view to legislation on these matters at an
early date."

4. It was clear then, and it is clear now, that we should want
to remove the uncertainties in this field as soon as possible,
and I have envisaged the 1980 Budget as the occasion. This
assumption has meant that it would be impossible to go through



a full Green Paper - Select Committee process of consultation; nonetheless we have invited and received submissions from a great many quarters.

5. The main constraint on action is now likely to be the revenue cost - and political difficulty - of a full-scale reform of the capital taxes in a year when tax reliefs will generally be very hard to come by.

6. There are five taxes which are either charged on capital or which are directly related to the ownership of capital. The present yield and manpower requirements are approximately as follows:-

	Yield £m	Staff
(i) Capital Transfer Tax	360	1,235
residual estate duty	25	
(ii) Capital Gains Tax	385	1,050
Individuals Companies	215	
Total	600	Not quantifiable
(iii) Investment Income Surcharge	215	300
(iv) Stamp Duties	550	380
(v) Development Land Tax	35	185

7. Much of the damage done by these taxes is caused by their number and by the fact that they interact haphazardly. I have therefore approached our recent review with the aim of eliminating one of them entirely, and I should naturally like to make substantial reductions in the others.

8. Development land tax and stamp duties can be disposed of quickly. In the case of the first I think we should stick to the line set out in "The Right Approach to the Economy" in 1977:

"We accept that capital gains resulting from planning permissions are in a category of their own and require special treatment."



In the recent Budget we cut the rate and removed the rougher edges of this tax and we may have a little more trimming to do. But in general I think the property development sector will be best served by a spell of fiscal stability, and I said so in my Budget Speech. Stamp duties one would like to reduce - both in house purchase and on investments - but I think this is something to be decided when we have a clearer idea of the budgetary position as a whole.

9. That leaves us with a choice of three taxes for elimination: investment income surcharge, capital transfer tax or capital gains tax. The choice is not an easy one but after examining them exhaustively with Treasury colleagues, I have made up my own mind that it is IIS that should go.

10. Capital transfer tax started out as a sharp political weapon. Since its introduction, however, we have succeeded in having it amended substantially. The tax was represented by 34 sections in the 1975 Finance Act. Subsequent amendments run to 71 sections. Relief for agricultural property now extends to a reduction of 50 per cent in the value brought to assessment, while in the case of business assets the 30 per cent concession introduced in 1976 was extended to 50 per cent in the following year. And, of course, because the reliefs are applied to assessment values, there is an effective reduction in amounts of tax payable averaging some 70 to 75 per cent. Meanwhile numerous reliefs have been introduced for trusts and for the heritage and the rate on lifetime gifts is half that on death over much of the range. We have other improvements in mind (paragraph 14 below). There has been a legacy duty continuously since 1796 and I think we got it about right in "The Right Approach to the Economy" when we said:-

"We would not think it right to remove all restraints on the aggregation and transmission of substantial wealth. It is no part of our aims to encourage the concentration of the country's assets in fewer and fewer hands. We are deeply concerned to enable many more people



to acquire and transmit property through the reduction of penal imposts on incomes, savings and transfers."

In these circumstances, I do not think that we should today contemplate abolishing CTT, since I do not think there is a sufficiently strong case for any of the alternative forms of 'death duty' to justify the upheaval that would be caused by replacing it.

11. There remains the choice between abolishing CGT and abolishing IIS. We have debated this at length within the Treasury - and indeed with many outsiders.

12. Capital gains tax has operated very unfairly during the recent inflation, and the Inland Revenue have examined the two possible solutions - indexation and tapering - pretty thoroughly. On this basis, our predecessors decided that neither change could be implemented without severely cutting the yield of the tax, while at the same time requiring more staff and so hugely increasing the proportional cost of collection. We have concluded similarly. The yield would be reduced by five-sixths to about £100 million; but we should need an extra 300 staff. Nevertheless I find it difficult to argue that genuine capital gains should be exempt entirely from taxation. Too often they represent the capitalisation of income and I believe we would lay ourselves open to the charge of inviting tax avoidance if we were to remove the tax altogether; the Opposition would almost certainly pledge themselves to reintroduce it. Our suggested solution, therefore, is to raise the CGT threshold very substantially to £5,000 (from £1,000). This allowance would run all the way up the scale. It would not effectively be withdrawn by a marginal provision as at present. This will exempt from the tax about three-quarters of the people now affected by it each year, with a consequent staff saving of 550.

*i.e. the
lower you
hold the
asset, the
less CGT
you pay.*

P.



13. That leaves us with abolition of investment income surcharge which can, I believe, be justified on both theoretical and practical grounds. There is, I think, much less case today for levying a higher rate of tax on investment income than on income from earnings. Whereas in the past investment income was deemed to be more secure than earned income, that is no longer the case; inflation has bitten deep into private capital and into the income derived from it. Removal of IIS will be particularly helpful to the elderly, who account for approximately a half of its total yield; it will remove a damaging disincentive to saving and enterprise, and it will remove distortions in the economy. The loss of revenue, at £215 million on a 1979/80 basis, will be rather less than in the case of the other two taxes, but there will be an economy of approximately 300 staff.

14. I now return to our detailed CTT proposals, which will between them save up to 525 staff. These are:-

- (i) to raise the threshold from £25,000 to an indexed £60,000 - or, if we do not index it, to £70,000. This will again reduce the number of individuals affected, by up to three-quarters;
- (ii) to cut the rates at all levels, with a scale running to a top rate of 60 per cent on estates over £2 million;
- (iii) to abandon lifetime cumulation and cumulate gifts for ten years only;
- (iv) to increase the annual exemption from £2,000 to £4,000;
- (v) to give a measure of relief to agricultural landlords.



In addition, it is essential that we find a way of ensuring that both CGT and CTT are not charged on the same gift at the same time, as sometimes happens now.

15. With all these steps, which will between them very substantially lighten the load, we need not also improve the reliefs for businesses which we persuaded our predecessors to make; as I said in paragraph 10 although expressed as a relief of 50 per cent of the value of the property charged, they do in fact cut the burden by 70 - 75 per cent on average. Peter Walker is content with this approach in relation to farmers where similar considerations apply. But he does want us to give a measure of relief to agricultural landlords, who at the moment do much worse than farmers in many tax respects. I think this is reasonable and that we should put landlords on broadly the same footing as farmers for CTT, bearing in mind the differences between them, and particularly the effect on the tax charge of the lower value that let land commands. We must also look to the commitments we have made on the treatment of forestry and the heritage.

16. The main elements of the package are thus:-

	Full Year Cost	Staff Saving
IIS - abolish altogether	£215 m	<u>300</u>
CGT - exempt the first £5,000 gains in each year (£2,500 for trusts)	£100 m	550
CTT - as in paragraph 14	£265m-£290m depending on threshold	425-525
CGT/CTT overlap - remove year	small	-

Amc.

The full revenue cost of this set of proposals would be about £600 million and the staff saving some 1,300. In the first year only the CTT changes would result in a loss of revenue - some £125 million. The other changes would not affect tax receipts until the following year.



17. All this can only be provisional at this stage. While I should like to be able to go further in lightening the burden of capital taxes, the budgetary prospect for the next year - and, as far as I can tell, for the year after that as well - does not look like providing much scope for further reductions in the income tax. There must, therefore, for presentational and budgetary reasons be a limit to what can be done about the capital taxes in the 1980 Budget. It is possible that I may not be able to go even as far as I have outlined above.

18. I know you will want to think about this, and you may want to discuss it with two or three of us. In the meantime I have authorised planning and the drafting of legislation to go ahead on the basis I have described.

A handwritten signature in black ink, appearing to be "G.H.", written in a cursive style.

(G.H.)

12 December 1979

12 DEC 1979





10 DOWNING STREET

From the Private Secretary

Sir Kenneth Berrill

I have now written to the Treasury about the question of corporation tax, and bank lending to the corporate sector. (I enclose a copy of my letter.) The Prime Minister would be grateful if the CPRS would also follow up this point with the Revenue.

I. P. LANKESTER

5 December, 1979.

98

c.c. Sir K.B. 21



10 DOWNING STREET

From the Private Secretary

4 December 1979

Dear Tony,

The Prime Minister has expressed concern that one factor behind the pressure for higher interest rates may be encouragement through the tax system for companies to borrow more than they otherwise would. To the extent that this borrowing is to finance unnecessary stock-building or excessive pay settlements, it is clearly undesirable. She is of course aware that the Chancellor of the Exchequer has commissioned a review of corporation tax and would be grateful if this aspect could be kept in mind in the review.

Yours ever,

Tim Laker.

Tony Battishill, Esq.,
HM Treasury.

21

PRIME MINISTER

At the meeting on monetary policy a fortnight ago you expressed concern that interest rates were being pushed up unnecessarily by companies borrowing for tax advantages.

As you know, the Inland Revenue are currently reviewing the structure of corporation tax. I understand two main issues are being considered:

i) Whether to change the imputation system under which the shareholder gets partial credit against personal tax for corporation tax paid by the company. Changes in this system can affect the attractiveness of borrowing as against equity capital for a company.

ii) Whether to change over to taxation of profits on a current cost accounting basis. At present profits are taxed on a historic cost basis but with very generous reliefs for capital expenditure and stock appreciation. These may in some cases encourage a company to borrow more than it would otherwise have done in order to benefit from the reliefs.

Any reduction in company borrowing would be generally undesirable if it reduced capital spending. But to the extent that it cut down on unnecessary stock-building and on excessive pay settlements, it would be beneficial.

I think it would be worth ensuring that your point is covered in the review. If you agree, I shall write to the Treasury as per the attached.

I will also ask the CPRS to follow this point up with the Revenue: CPRS have a good tax man at the moment.

570
SIR KENNETH BERRILL

c Mr Downey
Mr Crawley
Mr Guinness
Dr Rickard
Mr Hartley

Q1 0145

Mr. Hartley to see
Sir Kenneth Berrill
May thanks. I have
done on the draft which
was attached to this, and -
if the PM agrees - will be
writing to the Treasury
tomorrow.
DB

REVIEW OF CORPORATION TAX

I attach a note I wrote on 5 July. I have no later information. 4/12

Clearly, if the Prime Minister is concerned that the tax system is in some way encouraging excessive company borrowing and pushing up interest rates, this should be fed into the Revenue's review. However, it is not easy to draft a note for Number 10 without being certain what precise problem the Prime Minister has in mind.

Firstly there is the question of whether we actually have more borrowing than is desirable. Others will be more competent to comment than I, but I had always understood British companies borrowed rather less than our more successful competitors. I gather the Prime Minister's concern is that the tax system encourages companies to borrow more than they otherwise would, and that, if the money supply is to be held steady, this leads to interest rates higher than they would otherwise have been, which penalises non-business borrowers (especially mortgage payers). It is important to bear in mind that if this effect exists it cannot be harming business investors since the interest rate is being pushed up by their excessive demands. Put another way, if a tax penalty is placed on borrowing firms will be faced with bills which are as high as if the tax system had been left unchanged and interest rates had gone up. So one is effectively penalising firms to help house buyers. Moreover, it must be doubtful in a world without exchange controls whether reducing UK company demand for funds will significantly reduce interest rates.

Perhaps more important for the Revenue, however, is to know what balancing adjustment we want companies to make to compensate for reduced borrowing. They could reduce their investment - principally in capital assets or stocks. I would not have thought we wanted to discourage capital investment; I do

not know whether stocks are in any way undesirably high. Or they could raise capital by new equity rather than borrowing. Or (perhaps the most desirable option) they could reduce their operating expenses - especially by holding down wages - and replace borrowing with internally generated funds. This seems a pretty unrealistic hope. If tax penalties are intended to lead to reduced interest rates, the net extra pressure on companies to keep down wages is not likely to be very great.

Which objective we have affects which bit of the tax system we want to change. If we want more equity investment then the area to look at is the difference between the tax treatment of dividends and interest for companies. The imputation system of corporation tax reduced the difference in cost but still leaves loans as a cheaper form of capital looked at from the point of view of a company trying to give its investors equal after tax incomes. To give a shareholder £100 of taxable income, a company has to make £146 of profits - paying £76 in corporation tax and £70 dividend, on which the shareholder gets a tax credit of £30. To give the same benefit to a debenture holder the company only has to pay £100, as interest is deductible in full for corporation tax. The Revenue are including this question in the CT review but are not likely to push it hard without a major impetus from outside. However, for the CPRS to push this we would need to be clearer of the economic benefits than I am at the moment.

If however, the expectation is to reduce stocks or capital investment (or operating expenses) then the possibilities to look at are removing the deductibility of business interest or reducing the reliefs for capital investment or stocks. The first seems a non-starter to me. Bank interest is deductible on the same principle as any other business expense. Various lobbies press from time to time for deductibility to be removed for various business expenses which they feel are economically or socially undesirable eg. advertising. These proposals are always resisted stoutly by the Revenue on the grounds that they would make a nonsense of having an income^{/tax} system. Moreover, there is no distortion - it only pays a company post-tax to borrow if the pre tax profits from what it does with the money are higher than the pre-tax interest costs.

There is, however, a case for reducing the generous tax reliefs for capital investment and stockbuilding. Indirectly, these may be leading to excessive borrowing if it becomes worth a firm's while to borrow to invest more than it otherwise would have done just to get tax relief. In the case of stock relief any distortion is unintentional - it is a crude administrative device for approximating to current cost accounts and may in some respects be over generous. Generous capital allowances partly reflect the fact that they are based on historic costs rather than replacement costs but are partly a deliberate attempt to jack up capital investment beyond what it would otherwise be.

The Revenue's review is looking at the possibility of replacing both these reliefs with a more sophisticated current cost accounts basis but the government will want to think twice before removing all bias in the system towards investment in plant and machinery.

Further work is necessary before we could advise the Prime Minister which way the Revenue's review ought to be steered and to do this it would be helpful to talk to the Revenue and Treasury. They are, however, not likely to be forthcoming unless the Prime Minister gives some backing to the CPRS involvement. I have drafted a fairly low key note for the Prime Minister to send to the Chancellor of the Exchequer and would suggest that, if it is sent, I should then get in touch with the revenue to say that we have been asked by the Prime Minister for a view.

MJ

M A JOHNS

13 November 1979

01.070

MR. DOWNEY

cc Sir Kenneth Berrill
 Mr Crawley
 Mr Hartley
 Mr Guinness

CORPORATE TAXATION

Following our discussion on corporate taxation with Messrs Hoskyns and Strauss, I rang the Revenue (Mr Isaac) to see exactly what the scope of their review would be. The Revenue have not yet discussed this with the Chancellor and are in the process of putting up a note to him asking for guidance. One issue is whether to change the imputation system (giving credit to the shareholder at the basic rate for corporation tax paid by the company). The Revenue do not believe any conceivable benefits would be worth the cost of change. Companies certainly would not welcome another upheaval in the structure of the tax (2 previous ones in 1965 and 1972).

The other issue is what the correct measure of profits is. This raises questions like -

1. Should the tax base be adjusted to the ED 24 inflation-adjusted definition of profits? (How does this fit in with the treatment of inflation in other areas of the tax system?)
2. Should capital allowances remain at 100% in the first year?
Should they be based on replacement costs rather than historic costs?
3. What is the future of stock appreciation relief?

The Chancellor had laid down as a prerequisite of any system of inflation adjustment that it should be objective, equitable and simple to administer.

The Revenue thought the first stage was to get Treasury Ministers' views. The Chancellor would then have to discuss with the Prime Minister which other Ministers should get involved and how. The Revenue did not believe it could be helpful to put Treasury Ministers' decision in commission although there would have to be consultation of colleagues and, in due course, of outside interested bodies. It was particularly important to avoid the chaos of the last ten days over the Secretary of State for the Environment's initiative. It emerged that there was no question of the Treasury rather than the Inland Revenue taking the lead.

MAJ

(M A JOHNS)

5 July 1979.

016

July 1979

MINISTERIAL SPEAKING NOTE ON TAX CUTS

(Background Note attached)

Last month Geoffrey Howe introduced a Budget designed to tackle Britain's two basic economic problems:

low productivity
high inflation

To help get productivity up, he cut income tax dramatically:

basic rate down by 3p
allowances up by twice what was expected
top rate slashed

These cuts are aimed at restoring incentives to work and enterprise. But they are made within a strict financial framework designed to get inflation down on a permanent basis.

Both problems - inadequate productivity growth and persistent inflation - are deep seated: the turnaround will take time. But a start has been made and this week wage earners see the first fruits.

Improving incentives

Every married man on basic rate gets a rebate of £26.70. And he will pay £1.80 less a week after that. For a single man the figures are £17.10 and £1.10. That's the first picking.

In October a married man on about the national average of £100 a week gets a further rebate of £41.00. And his weekly wage packet will be fatter by another £1.50. At the same time the higher thresholds are changed.

Incentive for skilled workers to put in extra hours. Incentive for managers and professionals to stay and work for Britain.

Incentive for the lower paid - 1½ million are taken out of the tax net altogether.

Of course these tax reliefs have to be paid for: that's the financial discipline side of the Budget. Indeed, the Chancellor's

task was made harder because public spending and borrowing were already overshooting planned targets.

He faced up to this by cutting public spending and increasing VAT. But this is not - as some would have it - simply robbing Peter to pay Paul. That jibe completely misses the point.

By taxing what people spend rather than what they earn we are returning choice to the individual. He can decide what to spend his money on

- on a new hi-fi
- on a wider variety of food (which like other essentials is not taxed)
- or indeed to save it

rather than have the Government make the decision for him.

Because Government has grown too big, the incentive to hard work has been blunted. Too much has been taken from the wage packet in taxes. We cannot have a higher standard of living, we cannot enjoy better public services, we cannot command the full respect of other nations unless we improve the performance of our economy - unless, in the jargon of the economists, we transform 'the supply side'.

Checking inflation

But our efforts to improve the 'supply side' of the economy will come to nothing unless we can check inflation

runaway prices curb investment in new jobs
runaway prices destroy existing jobs
runaway prices lose orders and jobs to
foreign competitors
runaway prices undermine confidence and
the will to succeed

So this Government is determined to lick inflation. It will not be done overnight - there are too many forces, like the recent oil price rises, pushing in the wrong direction.

But we shall not print money to finance inflation. And this means that employers and employees must bargain sensibly if the country is to make the turnaround fairly painlessly. If firms pay more than they can afford and thus increases prices beyond their competitors, they will go out of business. If employees, already with tax savings in their pockets, use their muscle to push firms in this direction, then they will be putting their jobs at risk.

If, on the other hand, we all behave responsibly instead of pulling ourselves apart - as we have done too often in the past - we can move decisively in the right direction.

The Budget and pay claims

Some people are saying that the Budget, by pushing up the cost of living through the increase in VAT, justifies trade unions pushing for much higher pay. They are quite wrong about this. Taking account of the income tax reductions as well as the indirect tax increases, a family on average earnings will be better off over the period between the Budget and the end of the financial year. They will be paying about £2.75 a week more for what they buy (3½% on the RPI) because VAT and oil duty have gone up. But they will have about £4 a week more to spend (equal to 5½% on the RPI) because of the income tax reductions.

The German example

People sometimes envy the success of the West Germans. Well, they have avoided the trap of too much government and too high personal taxes; they have allowed the market to flourish; and they have encouraged people to work hard for themselves and their families instead of for the government; they have refused to finance inflation; and they have succeeded. Everybody is better off.

There is nothing to stop Britain going the same way if we have the will. It cannot happen overnight: we have got to work at it. It will be hard going for several years: but, if we are sensible it need not be painful.

The Government will play its part. The changes in the Budget signalled the way we are going to proceed. They increase people's liberty - liberty from too much Government interference: liberty to exercise a greater degree of individual choice. And, in doing this, they help create the right climate to produce the effort, the enterprise and the excellence which can make Britain thrive again.

BACKGROUND NOTE ON TAX CUTS

Effect of cuts

1. The three major changes to personal income tax (including the changes to allowances in the short pre-election Finance Bill) are:

- (i) single person's allowance up from £985 to £1165
married allowance up from £1535 to £1815
- (ii) basic rate reduced from 33 to 30 per cent
- (iii) higher rate reduced to 60 per cent and thresholds widened

<u>%</u>	<u>1979/80</u> £	<u>1978/79</u> £
40	10,001 - 12,000	8,001 - 9,000
45	12,001 - 15,000	9,001 - 10,000
50	15,001 - 20,000	10,001 - 11,000
55	20,001 - 25,000	11,001 - 12,500
60	Over 25,000	12,501 - 14,000
65		14,001 - 16,000
70		16,001 - 18,500
75		18,501 - 24,000
83		Over 24,000

2. The changes take effect in two bites

- (i) Changed allowances take effect on first pay day after 12 July.

<u>Examples</u>	<u>Single</u>	<u>Married</u> (wife not working)		
<u>Weekly</u> <u>Earnings</u>	<u>rebate</u>	<u>continuing</u> <u>weekly</u> <u>reduction</u>	<u>rebate</u>	<u>continuing</u> <u>weekly</u> <u>reduction</u>
£60	£17.10	£1.10	£26.70	£1.80
£100	£17.10	£1.10	£26.70	£1.80
£150	£17.10	£1.10	£26.70	£1.80

- (ii) Reduced basic rate and changes to higher bands take effect after 5 October.

<u>Examples</u>				
£60	£18.80	£0.70	£ 8.60	£0.30
£100	£51.20	£1.90	£41.00	£1.50
£150	£91.70	£3.40	£81.50	£3.00

(iii) Combined effects

<u>Weekly Earnings</u>	<u>Single</u>		<u>Married</u> (wife not working)	
	<u>rebate</u>	<u>continuing weekly reduction</u>	<u>rebate</u>	<u>continuing weekly reduction</u>
£60	£35.90	£1.80	£35.30	£2.10
£100	£68.30	£3.00	£67.70	£3.30
£150	£108.80	£4.50	£108.20	£4.80

3. A reminder of tax cuts per se can only be helpful in the context of forthcoming wage negotiations. However there are a number of problems.
- (i) we should avoid suggesting that everyone will be better off: they won't and can't until output starts expanding again. And it will be only too obvious - particularly if mortgage interest rates go up
- (ii) we should avoid presenting the July effects alone which will look pathetically small against some of the price rises: indeed this may present a platform for predictable attacks on the Budget strategy
- (iii) there will have to be some references to the higher rates - where the size of the rebates will only strengthen the view of those who regard the tax proposals as 'unfair'. Gallup findings suggested that about half of the country already so regarded them
- (iv) we must avoid the suggestion that better times are just around the corner: this could only lead to rapid dis illusionment and reaction against the whole strategy
4. Thus the proper approach is to present the two tax cuts together and as part of the overall economic strategy, viz
- (i) we cannot enjoy higher standards of living etc without sustained economic growth
- (ii) the strategy aims at tackling the two chronic problems inhibiting growth -
low productivity and
high inflation

(iii) the tax cuts are a first step to re-invigorate the 'supply' side of the economy and improve productivity

(iv) simultaneously we have to squeeze inflation out of the economy: this can mean temporarily unpleasant measures like high MLR and consequent high interest rates all round

(v) thus no quick turn around - problems are too deep-seated and compounded at present by oil price increase

(vi) if strategy works, we shall get on to a 'virtuous circle' as W. Germans and enjoy the kind of steady growth rate which they have experienced

(vii) but Government can only do so much - basically depends on will of the people

(viii) first major test with next wage round. If negotiators - despite tax cuts - insist on wage increases unrelated to increased productivity, it can only put jobs at risk and delay recovery of economy and real increases in standard of living.

5. Positive points

Switch from direct to indirect taxation.

1. In terms of the budget measures alone virtually everyone will be better off if the switch has been carried out in a fair way (VAT is not regressive - see below). A married couple with husband on near average earnings will have an average of £4 extra a week for the remainder of the financial year: price rises from VAT and oil duty increases are likely to cost them about £2.75 a week more.
2. The switch provides more liberty and choice for the individual. He can decide what to spend his money on - or indeed save it - rather than have the government decide it for him.

3. It is a vital part of the Government's strategy to stimulate the supply side of the economy. There has been no shortage of demand. Last year we produced only 1% more manufactured goods despite the boom in spending: the gap was filled by an increase of 13½% in the volume of imported manufactured goods.
4. No one can be sure that such a switch will achieve the results. But it removes obvious constraints to greater effort - including easing the crippling marginal rates. And most of the countries which have done conspicuously better than us have a large proportion of revenue coming from indirect taxes like VAT.
5. VAT is a fair tax in that it excludes essential items of expenditure: food, childrens' clothing, heating and lighting, housing, public transport. Averaged over all expenditure, the rate is equivalent to 8 per cent which is still almost the lowest in Europe.
6. Pensioners and others on social security benefits are protected from these price rises by the largest-ever increase in benefits - substantially larger than those proposed by the previous government before the election.

General economy

7. Higher standards of living can only come through higher output. Despite North Sea oil, industrial output last year was scarcely higher than 1973. The outlook (not helped by the oil crisis) is not significantly better. Radical action is needed.
8. The twin problems are low productivity and high inflation. They are deepseated and cannot be turned round overnight. But it is necessary to make a start immediately. Once they are overcome, there is no reason why we should not enjoy the kind of sustained growth that West Germany - pursuing similar policies - has obtained since its post-war recovery.

9. The speed and ease of the turnaround will depend very much on how individuals respond. If they look for higher earnings out of higher productivity and profitability then the timescale can be quite short. If (despite the tax savings) they insist on rises quite unrelated to their firms' performance, they must inevitably put their own jobs at risk and retard the nation's recovery. The Government is determined not to bail out concerns that get into financial difficulties because of irresponsible pay awards: that would be totally contrary to the aim of curbing inflation.

6. Defensive points

Price rises greater than tax cuts plus pay rises

1. This may be true in the short term - particularly because of the latest round of oil price increases which - by themselves - must reduce living standards. We cannot get overall improvement in standards until output starts expanding again: how quickly that happens depends vitally on how people respond to the tax cuts and how responsibly they bargain in the forthcoming pay round.

Tax changes unfair - wealthier get most/suffer least

2. Acknowledged widely - including by member of opposition when in government - that higher bands had severe disincentive effect on management and many higher skilled workers and contributed to drain of talent from UK.
3. Our new top rate of 60 per cent compares with 60 per cent in France, 56 per cent in West Germany and 50 per cent in the US. Our top income groups are generally still more highly taxed with those in our main competitor countries.
4. Over three quarters of income tax relief this year represents cost of increasing personal allowances and reducing basic rate.

Poorest hardest hit?

5. Pensioners and others on social security benefits protected

by benefit increases.

6. 1.3 million of lower-paid taken out of tax.
7. VAT not regressive - essentials excluded
8. Pensioners and low income groups exempt from eg prescription charges.

Foolish to put up MLR - effect on mortgage rates etc

9. The Government wants to get interest rates down as soon as possible. But top priority is to curb growth in money supply as prerequisite for cutting back inflation. Money supply was moving out of control immediately before the election; and interest rates must remain high until government is in control of money supply again.

Why need to suffer with North Sea oil?

10. Even with growth of North Sea oil, industrial output has hardly risen in total over last 5 years - ie manufacturing has actually fallen over this period. Thus North Sea oil is doing no more than disguising an industrial decline.
11. If no action taken now, decline likely to continue. When North Sea oil runs out we shall be impoverished and suffer a rapid decline in living standards.
12. Must use North Sea oil as an opportunity to reverse decline before it is too late.

Need for public expenditure cuts?

13. Generally, the Government believes that the public sector is too large and needs to be curtailed if enterprise is to flourish and new wealth created. It is a question of getting the balance right; and at present it has swung too far one way. Too great a public sector reduces private initiative both by creating too heavy a tax burden and by trying to solve too many problems for individuals and firms.

14. Specifically, public expenditure has been increasing faster than the country can afford. Plans assume and have assumed economic growth beyond what has been or is likely to be achieved. Where it is appropriate for the public sector to provide services the Government wants to see them improved: but this can only happen when the country can afford it. If public expenditure expands without corresponding national economic growth, it can only be at the cost of starving the private sector of resources.

Paymaster General's Office
Privy Council Office
68 Whitehall
London SW1

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010
C. A. Whitton
Prime Minister ECA PL 2
To note. I will
check this up in
the autumn.

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

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24/7

PRIME MINISTER

BF
10/10/79

We spoke briefly the other day about the scope for raising extra revenue in 3 areas -

- Leasing
- Stock relief
- Perks

2. We have a review of leasing under way. I hope to have its Report in October, in good time to consider the options and take any necessary action in the 1980 Finance Bill.

3. The future of the stock relief scheme raises rather wider issues and, in particular, is tied in with the whole problem of inflation accounting. I see it as a main element in the review of corporation tax which I promised in my Budget Statement. A good deal of work is in hand and we shall want to consider further in the autumn the options and the timetable for future action.

4. We are reviewing the whole question of the taxation of "perks", with particular emphasis on company cars and on the possibility of applying the tax charge to all employees (not only the higher paid) and requiring the employer to deduct tax under PAYE. At this stage we have

/it in mind

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it in mind to increase the company car scales substantially with effect from next year, and to bring forward other measures which would not take effect before 1981-82. This is an area that is, as you know, fraught with difficulties on the frontier between principle and practice. I am therefore taking particular care to "get it right" before proceeding with definite proposals.

gm

(G.H.)

24 July, 1979

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24 JUL 1979

Orig: Garden Room

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CF GJR

10 DOWNING STREET

THE PRIME MINISTER

20 July 1979

Dear Mr. Plastow,

I am grateful to you for your letter of 18 July, recording your Committee's reaction to the Budget and the economic strategy which underlies it.

I am delighted to see this positive response, and I shall of course pass your comments to Keith Joseph — and will use them in speeches and Parliamentary Questions myself.

Yours sincerely
Margaret Thatcher

D.A.S. Plastow, Esq.

HTS

Original: Gordon Brown



10 DOWNING STREET

PRIME MINISTER

This letter from the Society of Motor Manufacturers and Traders is a positive response to the Budget.

Would you like to acknowledge as in the attached draft? I will then pass the letter to Sir Keith Joseph's office.

MAD

C.R.
Copy to A. Duguid in
Sir K Joseph's
office, with
incoming letter, pl.

19 July 1979

MAD

Orig: Garden Rooms

from the: Deputy President - D.A.S. Plastow

The Society of Motor Manufacturers and Traders Limited Forbes House Halkin Street London SW1X 7DS Telephone 01-235 7000
Registered Number 74359 England Registered Office

18 July 1979

The Rt. Hon. Margaret Thatcher, MP
Prime Minister,
10 Downing Street,
London S.W.1.

Dear Prime Minister,

At the Society's Executive Committee meeting this morning - at which I took the chair in the absence of our President, Sir Barrie Heath, who is ill - I was asked to advise you of the Committee's unanimous agreement that:

1. We are surprised at the criticisms of the Government Budget strategy from some other parts of the private sector.
2. The Budget provides a degree of incentive which will encourage men and women at all levels in industry to produce the extra effort and the initiatives which are essential to this country's economic revival.
3. Management in the motor industry will certainly play its part in striving for the improved productivity and international competitiveness which are vital to the industry's recovery.
4. We look forward to a new relationship between industry and Government in which Government does not seek to intervene in the day-to-day management of industry, but:
 - spells out clearly what is expected from all concerned with industry, including both management and trade unions;
 - identifies and agrees with industry the economic objectives to be pursued within the UK economy and in our international trading relationships; and
 - recognises industrial efficiency and growth as a major priority in its fiscal, social and legislative policy decisions.

*Yours sincerely,
David Plastow*

Top Copy
European Policy
March 79 - A Council Policy by 3 wise men

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Rule 114
GMA 177
GMA 114

NOTE OF THE PRIME MINISTER'S DISCUSSION WITH THE COMMITTEE OF THE
THREE WISE MEN AT 10 DOWNING STREET ON 16 JULY 1979 AT 1015

Present: Prime Minister Mr. Barend Biescheuvel
Foreign and Commonwealth Secretary Mr. Edmund Dell
Mr. Michael Franklin (Cabinet Office) Monsieur Robert Marjolin
Miss Alison Bayles
Mr. B.G. Cartledge

The Commission

After welcoming the Committee, the Prime Minister commented that the remit which they had been given by the Presidency was very vague. She herself was only just beginning to understand, in the light of practical experience, how the Community worked. The Prime Minister said that she thought that one effect of the enlargement of the Community would be to diminish the amount of effort which was devoted to "harmonisation", which all too often meant standardisation. The European Commission had, in her view, concentrated excessively on harmonisation, whereas one of the great virtues of the Community was its variety. Enlargement would bring a greater sense of perspective. The directly-elected European Parliament, moreover, would have a significant effect on the Commission's operations, although it remained to be seen to what extent the European Parliament would devote its attention to internal matters. It had to be recognised that the Parliament might swell the Community's bureaucracy.

Mr. Biescheuvel recalled that his Committee had been nominated by the European Council at the end of 1978 and asked to consider adjustments to the machinery and procedures of the Community's institutions. He and his colleagues were also charged with safeguarding progress towards European union, in the context of the forthcoming enlargement. The Committee proposed to submit their report in October 1979. During the first three months of their work they had visited eight capitals out of the Nine, and the European Commission, their meeting with Mr. Callaghan having been postponed because of the British Election campaign. The drafting of their report was now under way.

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/Mr. Biescheuvel

Mr. Biescheuvel told the Prime Minister that he and his colleagues had encountered widespread criticism in the capitals of the Nine with regard to the way in which the Community's institutions functioned and concerning the lack of co-ordination between the Commission, the Council of Ministers and the European Council. The question of the co-ordination of Community work in each national capital, with the objective of producing clear guidance for national delegations, was also relevant to the Committee's mandate. The Committee were nevertheless very conscious, Mr. Biescheuvel said, that the major problems which faced the Community could not be solved simply through adjustments in procedure and mechanics. He was conscious, however, that the Committee had to take account of a problem which was preoccupying a number of people in the Community, namely that of what the Community should and what it should not attempt to do. During their enquiries, the Committee had been greatly struck by the difference in the economic environment which could be expected in the 1980s and that which they recalled from the 1960s. In tackling the problems which would result from this, the European Council might have a very important role to play, by giving clear political guidance as to which problems the Community should try to resolve and as to how this could be done.

Mr. Biescheuvel said that the Committee had also looked at the question of the co-ordination of the work of the specialised Councils. They thought that the role of the Foreign Affairs Council could perhaps be improved by strengthening the role of the Presidency. So far as the Commission was concerned, it clearly had a management role to fulfil and a supervisory function, in addition to its function of initiating legislation. The position of the Commission had in fact tended to weaken in recent years and he and his colleagues had discussed this question with the Spierenburg Committee. The two Committees were agreed that the Commission's work should be rationalised and that economies could be made. It had been suggested that the number of Commissioners should be reduced from 13 to 10: Mr. Biescheuvel said that he would welcome the Prime Minister's views on this.

/The Prime Minister

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- 3 -

The Prime Minister said that she for her part - although she had been briefed in the opposite sense - agreed with the view that there should be one Commissioner for each member of the Community. She realised that the advantage of having two Commissioners was that it was possible to achieve a party political balance between them. She nevertheless believed that this problem could be solved by choosing the right man to be a country's sole Commissioner. She would be happy to accept, for example, Mr. Roy Jenkins or Mr. Dell as the UK's Commissioner, although she could think of some members of the Opposition party who would be less acceptable. The alternative to ten Commissioners, however, was 17: this would be ridiculous. The Prime Minister said that she would be content for there to be one British Commissioner, so long as every other member of the Community was limited to one as well.

Lord Carrington said that he thought that the Commission has become less powerful as the role of the European Council had grown. Commissioners, therefore, had a less important part to play than had previously been the case. He agreed with the Prime Minister that the argument for having two Commissioners was that it was possible to maintain a political balance. Mr. Dell put the argument that the larger member states of the Community might have less confidence in a Commission on which they thought they were inadequately represented. Mr. Biescheuvel said that it was rather difficult to tell the smaller members of the Community that one Commissioner per member was sufficient on the grounds that the Commission itself had diminished in importance. He foresaw that the smaller members might wish actively to restore the powers of the Commission.

The Prime Minister said that she thought that the role of one Commissioner per member country could be defended entirely adequately on the twin grounds of equity and efficiency, just like the United States Senate. It was, however, for consideration whether the Presidency of the Commission itself should count as one of the ten national seats or whether it should be additional.

Mr. Biescheuvel told the Prime Minister that the Spierenburg Committee would probably recommend that the President of the Commission should be able to nominate a Vice President who could assist him in

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- 4 -

the responsibility for internal co-ordination and for the budget. Other Commissioners would have specific portfolios and the number of Directors General cut down. The Prime Minister said that the first principle should be to avoid any further increase in members of the Commission and the number of Directors General.

Lord Carrington pointed out that if the larger members were to have only one Commissioner a piece, problems would arise if these Commissioners were not allocated the most important portfolios. Mr. Dell suggested that the President might be given a decisive voice in the allocation of portfolios in the Commission so as to reduce the risk of the appointment of unsuitable or inadequately qualified Commissioners, whose Governments had put their names forward in order to get them out of the way.

The Prime Minister thought that if the President of the Commission were empowered to allocate portfolios, this would inevitably lead to ill feeling: such appointments could only be made by general agreement. Mr. Dell recalled that Mr. Jenkins had been appointed to the Presidency on the basis that he would definitely have a say in senior appointments. Despite this, however, a number of very unsuitable appointments had been made during his term of office, since he lacked any formal power in the matter. The Prime Minister said that she thought that the power to make appointments could only increase friction and distrust of the President. If each member were allowed only one Commissioner, they were likely to be even more careful about their choice.

European Council

The Prime Minister made the general comment that all the Councils met far too often. There should be fewer meetings,

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with properly prepared agendas and competent chairmanship. It was unnecessary for the European Council to meet three times a year. At the only European Council meeting she had attended so far, it had been necessary to pad out the agenda for the second day in order to use up the time. It should be quite sufficient for the European Council to meet once during each Presidency. The Prime Minister said that she thought that, quite apart from Community occasions, there was much too much summitry in the international calendar: this obliged Heads of Government to divert their attention from the national problems which should be their main concern. The Prime Minister made the further comment that a Presidency of only six months might be too short. Lord Carrington pointed out that if each Presidency lasted for a year, it would only come round to the members of the enlarged Community once in 12 years.

Mr. Dell asked the Prime Minister how she saw the role of the European Council. The Prime Minister replied that she thought its purpose was to deal with the major issues facing the Community, such as the CAP and the budget. The CAP, she said, was a protectionist mechanism which ran contrary to one of the basic principles of the Treaty of Rome, namely the increase of free competition.

M. Marjolin said that if the European Council was to be the Community's major source of political initiative and political momentum, it might be the informal parts of the Council's programme which had the most value. The Prime Minister acknowledged that this might be true in principle, but said that in practice the contributions made round the table by individual Heads of Government, even on the informal occasions, were very uneven: some Heads of Government rarely intervened at all. The Prime Minister went on to say that European Councils were accompanied by far too great a volume of paperwork: the outcome of the Council's discussions was always predictable but they were nevertheless preceded by an enormous preparatory operation. Discussions in the European Council tended to be woolly and generalised; the invariable decision was to "have some more work done" on the matter in hand. Bilateral meetings were sometimes more useful.

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/In further

In further general comment, the Prime Minister expressed the view that the CAP was appalling from an intellectual standpoint. She also pointed out that the tradition of equity which was so strong in the UK did not, evidently, prevail in Europe. In the Community, every member seemed to approach a problem by fighting his national corner.

Lord Carrington said that if the powers of the Presidency were increased there was a danger that they could be used for national interests and purposes.

Mr. Dell said that the European Council might work a little better if its secretariat were more effective. The Prime Minister said that it would be helpful if an agenda could be fully agreed in advance and then adhered to. Mr. Dell said that he and his colleagues had found general agreement in their consultations that the quality of the Council secretariat could and should be improved.

The Prime Minister said she had been appalled by the difficulty of drafting the European Council's conclusions in such a way as to reflect the decisions which had been reached. Mr. Franklin suggested that there should be a secretary to the Council who could give the definitive view as to what had been decided. At Strasbourg, the meeting of Foreign Ministers early on the morning of the second day had been a helpful innovation.

The Prime Minister said that she would wish to retain the power of veto (the Luxembourg Compromise): she was very wary of going over to the system of majority voting. M. Marjolin commented that the Prime Minister's views on the Luxembourg Compromise seemed to be generally shared, although it was important that the power of veto should not be abused.

European Parliament

The Prime Minister said that relations with the European Parliament should be handled exclusively by the Commission. The President should visit the European Parliament only in

CONFIDENTIAL

- 7 -

order to give an annual "state of the Community" message. Mr. Dell forecast that the directly-elected European Parliament would inevitably demand the presence of Ministers at its sessions. The Prime Minister commented that the Parliament could request but not demand. It was essential that the question of where legal responsibility lay, as between the European Council and the European Parliament, should be correctly defined and not blurred. The Council of Ministers had the final say. M. Marjolin commented that the question of the Commission's responsibility vis-a-vis the European Parliament was theoretical, since the Commission now had no power. The Parliament would be keen to go to the real source of power, namely the Council.

The Prime Minister pointed out that if the European Parliament wished to acquire power, the national groups within it would have to work in close co-operation with the members of their own national Parliaments, where the only true authority and responsibility lay. She said that she regarded the elected European Parliament as a catastrophe: the situation had been much better when the national Parliaments sent delegations. But she accepted that the direct elections had to take place.

Mr. Dell pointed out that the European Parliament did in fact possess some powers, for example, for the financial field. It would be necessary to establish some degree of liaison with the Parliament on such issues as, for example, the Community budget. The Prime Minister repeated that it should be sufficient for the President of the day to visit the Parliament once during his Presidency. Lord Carrington pointed out that Irish Ministers, during their Presidency, were clearly planning to spend a considerable amount of time in Strasbourg. The Prime Minister commented that what the Irish did need not constitute a precedent for anybody else. Lord Carrington said that it nevertheless made it more awkward for the Ministers of other member states to neglect the Parliament and Mr. Biescheuvel agreed.

/ Other Questions

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- 8 -

Other Questions

Lord Carrington suggested, and Mr. Biescheuvel accepted, that if the remaining questions could not be covered over lunch they might be put down on paper. In the few minutes remaining, the question of the two-speed Community could be considered.

The Prime Minister said that the two-speed Community was a fact of life. Lord Carrington commented that the two-tier division of the Community should nevertheless not be formalised since this would make convergence more difficult. The Prime Minister said that it would be dangerous to hold the faster members back. Mr. Dell said that a problem arising out of the two-speed Community was that the Community endeavoured to assist the slower members with subsidies which ran counter to the Treaty principle of the free flow of goods and services.

As the discussion ended, the Prime Minister expressed the view that more contact between the European Community and NATO was needed: there were too many demarcation disputes between them and it was absurd that we and other Community members should have three Ambassadors in Brussels. Lord Carrington pointed out that different plays required different casts.

The discussion ended at 1125.

bu.

16 July, 1979.

CONFIDENTIAL



Drainbridge 2

You asked how
much corporation
tax came from
manufacturing.

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

13th July 1979

Dear Tim,

DL
17/7

Following Tony Battishill's letter of 5th July you wrote on 9th July to ask how much of the 1978/79 yield of CT came from manufacturing companies.

We estimate that of the £m3,938 CT yield in 1978/79 given in the FSBR about £m1,700 came from manufacturing companies.

Yrs evr,

Mt
(M.A. HALL)

3,938 c.f.
2700

T. Lankester, Esq.,
No.10, Downing Street

11 12 1
10 9 8
7 6 5
4 3 2
1

16 JUL 1979



*Original
in R*

10 DOWNING STREET

THE PRIME MINISTER

12 July 1979

Dear Mr. Close,

Thank you for your letter of 6 July with which you enclosed a note on the Budget. I was most gratified to see that you have written to all your members urging them to make a positive response to the Chancellor's measures.

Yours sincerely,

(signed) M.T.

Roy Close, Esq., C.B.E.

Instit. of Br. Management.

tmw

def 16/7

9 July 1979

The Prime Minister has read your letter of 5 July, and on the subject of corporation tax and stock relief she has asked how much of the £4 billion which corporation tax yielded in 1978/79 came from manufacturing companies. I would be grateful if you could answer this point.

T.P. LANKESTER

Tony Battishill, Esq.,
H.M. Treasury.

pe

cc Campbell
✓ to the letter
to Hoskyns



Denis Heath 2

To note - progress
report on corporation
tax and 'standard of
living' index.

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

PH

5th July 1979

TL
6/7

Dear Sir,

Play A

In your letter of 21st June you asked for comments on points which the Prime Minister had made on stock relief and corporation tax. As a separate matter your letter also said that the Prime Minister had asked what progress was being made in devising a 'standard of living' index, which will include tax as part of the cost of living.

Corporation tax and stock relief

The Chancellor has already set in hand a wide-ranging review of the corporation tax system.

Although stock relief has undoubtedly provided a good deal of help for industry, it is true that it is rough and ready and can to some extent be manipulated. For this reason it is already being looked at as part of the review; the Chancellor will certainly take account of the Prime Minister's observations.

*How much
from manufacturing
corporations?*

Meanwhile, it would be wrong to understate the effectiveness of the corporation tax, although it is clearly uneven in its present form. It yielded nearly £4 billion in 1978-79, and is forecast to rise to nearly £5 billion in the current year. Certainly, it has been less buoyant than income tax. But this was in some aspects inevitable, with company profitability as low in real terms as it has been recently. Corporation tax remains the third largest revenue-raiser, after income tax and VAT.

Before bringing forward any proposals for change, the Chancellor will be consulting both with colleagues and with outside interests; and he will, of course, in due course be reporting to the Prime Minister.

/Development of

T. Lankester, Esq.,
No.10, Downing Street



Development of a tax and price index

As for a 'standard of living index' a group of officials, with representatives of the Treasury, CSO, Department of Employment and the Inland Revenue under Ian Byatt's chairmanship, was set up to consider this question some time ago. It reported to the Chancellor early in June. The group report concluded that while it would be unacceptable to consider ceasing publication of the retail prices index (RPI), or changing the basis on which it is calculated, there was a strong case for developing supplementary statistics which would reflect more adequately the effect on the purchasing power of households of changes in the balance between direct and indirect taxes. The most fruitful approach seemed to be to develop a "tax and price" index. This appeared to fulfill the essential objective of Ministers in that it is an indicator which takes account both of movements in retail prices and in direct tax liabilities.

The group's general approach has been endorsed by the Chancellor. He has however stressed that the objective should be to construct a single overall index, rather than a number of indicators relating, for example, to different household types, income levels, etc. Officials explained that a number of technical problems remained to be resolved and that the development of an overall index which would stand up to critical examination, and therefore be credible, would take time. Nothing of this kind would be available before the autumn. However, while work on an overall index would continue, figures for specimen households could be prepared quite quickly and should be available for publication in time for the July RPI (which will reflect most of the effect of the Budget package), due to be published in August, and well in time for the start of the coming pay round.

The Chancellor asked the group to follow up this work with all speed, emphasising the critical importance of getting the presentational aspects right. For the next stage of the exercise the group will carry out calculations to show (for specimen households) how the index would have performed in the recent past, in comparison with the RPI and earnings indices, and how it is likely to behave over the next 12-18 months. The group will concentrate on the presentational aspects of the index and prepare a draft press notice. They hope to complete this next stage of the work in about a week. Ministers will then be in a position to make final decisions about publication of the index. A fuller report on the characteristics and properties of the index will also be prepared.

Yours ever,
A. M. W. Battishill

(A.M.W. BATTISHILL)

6 JUL 1979



United States Double Taxation Convention

The clauses dealing with the UK-US Double Taxation Convention are purely of an enabling nature, and will only take effect when the Convention has been approved by affirmative order in the House of Commons. Hence the storm, that has been brewing over omission of the clause banning unitary taxation practised by some American states, will not break until later. Under the unitary approach, tax is levied according to a proportion of a multi-national's worldwide profits rather than on its local profits. Multi-national companies are opposed to the unitary concept, both because of the vast costs it can involve and also because they are loath to disclose confidential information about their world-wide operations. The clause banning unitary tax was dropped last year after a battle in the US over state and federal rights. The Convention, minus the clause, was approved by the Senate Committee and, unless the controversy surrounding the Salt-2 Treaty holds things up, it should pass through the House of Representatives quite soon. There are likely to be last minute attempts by major British companies to squeeze concessions, but these will not relate to the passage of the Finance Bill.

Small Businesses

Small Businesses will benefit in a number of ways from the Finance Bill:

- Income Tax Cuts—Lower income tax will help people wanting to save to start their own business.
- Corporation Tax—The profit limits qualifying small firms for the lower rate of corporation tax are increased from £50,000 to £60,000 at the lower limit and from £85,000 to £100,000 at the upper limit.
- Stock Relief—Small businesses will benefit from the general relief. In addition, the profit restriction for unincorporated businesses is reduced from 15% to 10%.
- VAT—Single-rate of tax helps cut the cost of operating the tax. Higher rate provides a temporary increase in cash-flow.
- Investment Income Surcharge—Raising the threshold for payment of the surcharge will help small businessmen retiring on income from savings.

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TIM. How often see us.

Westminster Industrial Brief

Finance Bill 1979

Special Issue

Contents

- Background to this year's Finance Bill
- Some of the amendments which have been tabled
- Some points relating to the Budget
- More detailed look at some of the changes affecting business

Westminster Industrial Brief
12/13 Henrietta Street
London WC2E 8LH

Telephone: 01-240 5289

July 4, 1979

Background

The Finance Bill 1979, which gives effect to Sir Geoffrey Howe's June 12 Budget, is the first Conservative Finance Bill for six years. In many ways it is untypical of any Government's most important piece of financial legislation. Published on June 21, only seven weeks after the Conservatives took office, it is slimmer than most predecessors. Since it must be passed before the Summer recess begins in late July, there are constraints on how much time can be given to debating it. Influencing the Budget was the fact that Whitehall is already a quarter of the way through the financial year and this imposed limits on how much could be done in such areas as public spending cuts. Nevertheless, the Finance Bill puts into effect a Budget considered to be the most marked turn-around since the War.

With the need to push the Bill through within five weeks, the usual parliamentary process has been cut short. Under normal circumstances, clauses and amendments are debated in the Committee of the whole House after the Second Reading debate, before moving 'upstairs' to the Standing Committee where it receives more detailed consideration. However, this year it is escaping the clutches of the Standing Committee and is only being debated on the floor of the House. This is the first time that this has happened since 1967, with the exception of Mr Healey's holding Finance Bill in April this year when all stages were concluded in one day before Parliament was dissolved. Although the Labour Opposition has pressed for more time, the Committee Stage is not expected to last for more than seven days, with only one day for the Report.

Because of its brevity and the unusual circumstances surrounding this Finance Bill, WIB is not publishing its normal clause-by-clause review of the Bill's progress. To a large extent this is unnecessary since, given the Government's majority, the Finance Bill should emerge relatively unscathed from the Committee Stage. Despite strong attacks from the Opposition parties, they have neither the time nor the muscle to instigate any major changes. Even with the Liberal Party voting against the Bill, as they did in the Second Reading debate, the Conservatives can count on enough votes of their own to defeat any major amendments to the Bill. The over-riding philosophy guiding Sir Geoffrey's hand was to avoid as many complicated legislative changes as possible, and the Government will apply the same attitude to attempted amendments. Even though the Labour Opposition has imposed a three-line whip on the Petroleum Revenue Tax and indirect tax clauses, there should be little difficulty in getting these through. Apart from the odd drafting amendment, the Finance Bill should emerge on the Statute Book virtually unchanged.

Tabled Amendments

Nonetheless, several amendments have been tabled. Even though Conservative backbenchers were encouraged by the Government to give the Bill a smooth passage and to refrain from putting forward amendments, many have been tabled from the Conservative benches. All the amendments to be debated during the first six days of the Committee stage relate to the provisions on VAT. The first day of debate on July 3 concentrated entirely on Labour amendments to the 15% rate of VAT. The second day dealt with attempts to exempt various goods and services affecting the disabled, registered charities and youth clubs and hostels from the increased rate of VAT. The whole of the third day of debate on Thursday July 5 was given to debating a joint amendment, tabled by such diverse characters as Bob Mellish and Edward du Cann, which attempts to exempt bloodstock and thoroughbred horses from the 15% rate. The fourth day of debate will deal with amendments relating to washing machines and laundry services, the fifth with exempting clothing and footwear from any increase in VAT, and the sixth with exempting from the increased rate repairs to buildings, including those of historical or architectural importance, and insulating materials designed to conserve energy. On the seventh day, both Liberal and Labour amendments to the rate of duty on light and heavy oil will be discussed, as will a Labour new clause attempting to change the rate of Vehicle Excise Duty from £50 to £40.

Various amendments which are unlikely to be discussed should be noted, if only for historical interest. A Conservative amendment, of interest to small businesses, attempts to double the turnover threshold for a business paying VAT to £20,000 a year. Nicholas Winterton, Conservative MP, has attempted to change the provisions on investment income surcharge. A Liberal amendment is aimed at indexing the £500 maximum value for individuals participating in Profit-Sharing schemes. Also, the 60% rate of Petroleum Revenue Tax is not considered high enough by the Scottish Nationalists who have made an attempt to get it raised to 75%.

A concerted effort has been made to get clauses concerned with raising or indexing the Death Grant added to the Bill. Despite the Chancellor's statement that measures relating to Capital Gains Tax and Capital Transfer Tax would need more time for consideration, some Conservative backbenchers have made a vain attempt to get these included in the Bill.

All in all, the tabled amendments are largely predictable and should cause few problems.

Budget Notes

As a whole, the Finance Bill reflects a bold Budget which, in effect, was a combination of two separate but complementary budgets dictated by the economic realities of Labour's legacy, together with the need to implement the Conservatives' election pledges. Thus, on the one hand, the need to keep a grip on the money supply and the PSBR necessitated the nasty medicine of raising the Minimum Lending Rate and indirect taxes so high. On the other hand, the substantial tax and public spending cuts were merely the first stage in implementing the promised switch from tax on income to tax on consumption, in order to restore incentives, and in reducing the role of the State.

Points on VAT

- The estimated revenue from the VAT increases for 1979-80 is less than half what is envisaged in a full year.
- The forecast revenue in a full year from the VAT increases is only £100 million short of the total envisaged loss of revenue from the income tax cuts in a full year.
- This increase in VAT income will provide Sir Geoffrey Howe with an extra £1.5 billion a year with which to manoeuvre next Spring without any change in the fiscal balance or further indirect tax increases.
- The impact of the VAT increases on the Retail Price Index is a once-and-for-all effect.
- About half the total of consumer expenditure is zero-rated or exempt from VAT (see Subscribers' Forum, February Issue). Poorer households tend to spend more on items in these categories than on those subject to VAT.

Points on Income Tax

- Sir Geoffrey Howe announced that it was his aim eventually to make the 25% lower rate of income tax the basic rate.
- Labour's introduction of the 25% "lower rate" tax bracket was attacked at the time as a gimmicky innovation which is disproportionately expensive to administer.
- With the actual rates for higher income tax now substantially reduced, the likely trend in future years will be the raising of the thresholds and the widening of the tax bands.

Point on Spending Cuts

- Some of the money gained from the cuts in the Regional Development Grant will come from deferring the subsidy payments for four months. As a result, £145 million will be cut from this year's PSBR and pushed into 1980-81.

Impact on Business

Despite the fact that it is the slimmest Finance Bill for many years, consisting of a mere 22 pages, it contains several important developments for business.

Stock Relief

Measures designed to patch up the existing system of stock appreciation relief have long been outstanding. Criticisms of the system as a whole still remain, and in his Budget speech Sir Geoffrey Howe

promised to reconsider the whole question of inflation accounting along with the accountancy profession's latest proposals on current cost accounting. For the present, the new measures fall into three categories:

- Write-off of Past Relief—In line with an undertaking given by the Labour Government, deferred tax liabilities arising from stock relief given for the first two years of the scheme (1973-74 and 1974-75) are written off, and thereafter liabilities in respect of each subsequent year will be written off after they have been outstanding for six years. It should be noted that, as a result of writing off the first two years in one go, most companies will have no write-off the next year. All in all, these measures will reduce the accumulation of large deferred tax liabilities relating to unrecovered stock relief.
- Amount of Stock Relief—In calculating the stock value on which relief can be claimed, the profit restriction is reduced from 15% to 10% for unincorporated companies. The new proposal goes some way towards meeting the criticisms of the existing scheme; it involves the minimum amount of change to the existing formula which accountants are now familiar with, but the criticism of the profit restriction itself still remains.
- Claims for Partial Relief—This enables businesses to claim stock relief in part or in whole as they desire, while carrying forward unutilised relief to future years. Under existing legislation the whole of the relief must be claimed for any period of account or none at all. The new measures for carrying forward unclaimed relief to future years go further than most people had anticipated.

The only significant omission from the provisions on stock relief is that providing relief for businesses which experience a dip in stock values. Under present legislation, a recovery charge arises subject to the amount of unrecovered past relief where there is a reduction on stock values. There has been pressure from industry for a scheme which includes an option for the deferment of a recovery charge for one year to meet the case where the fall in value of stock is a temporary occurrence which would probably be corrected in the following period of account. Companies suffering from the effects of last winter's industrial disputes are therefore unhappy about this omission. However, the Inland Revenue's view is that such action would be too costly.

Petroleum Revenue Tax

The main points are:

- Increase in the rate—In line with changes first proposed last year by the former First Secretary to the Treasury, Joel Barnett, PRT is significantly increased from 40% to 60% for chargeable periods after December 31, 1978.
- Reduction of uplift for allowable expenditure—The "uplift" in computing profits for PRT purposes, where allowable expenditure is taken into account, is reduced from 75% to 35% for expenditure incurred under contracts entered into after January 1, 1979. Expenditure incurred under contracts entered into before that date will attract the 75% uplift, whilst "alterations or additions" after that date to contracts made before it qualify for an uplift of 66.67%.

Oil companies are unhappy about these changes, since they argue that there was an undertaking in 1975 that PRT would not be increased or changed. Against this, the Inland Revenue has removed an anomaly from the original legislation:

- Extension of allowable expenditure—The valuation point for oil is shifted from the point of landing to that at which it can be realistically seen as saleable. Thus, transport and other such costs will be taken into account.

Other points include:

- reduction of the oil allowance for each field which is free of PRT
- metrication of measurements
- BNOC to be liable to PRT



10 DOWNING STREET

THE PRIME MINISTER

4 July 1979

ECM P1 10
CC HMT
DM
DOI

Dear John.

Thank you for your letter of 28 June.

I was very pleased to see the letter which you have sent to all your members. This is indeed very helpful and encouraging. The decision of RTZ to proceed with the Wheal Jane project, and also the excellent letter from Debenhams which you enclosed, are also most gratifying.

I look forward to seeing you next Monday, and I would be glad to discuss the whole question of getting over the message that wage claims must be responsible and realistic.

Yours sincerely
Margaret Thatcher

Sir John Methven

22000 PD
Original in GTR



CC HM
PHSS
MOD

JS.

10 DOWNING STREET

THE PRIME MINISTER

4 July 1979

Dear Mrs. Strange,

Thank you for your letter of 13 June.

It was most kind of you to write expressing your members' appreciation of the Budget announcement about war widows' pensions. It is a small change in terms of the Budget as a whole, but it is thoroughly deserved and I know that this is widely recognised. I am delighted to hear that it has given such pleasure.

Yours sincerely

Margaret Thatcher

Mrs. Iris Strange

War Widows Assoc.

⑤

PRIME MINISTER

28/6
I attach a draft reply for you to send to Sir John Methven - in response to his encouraging letter (Flag A). John Methven had already mentioned to me that the CBI delegation next Monday would like to discuss with you "the information problem" i.e. getting over to pay negotiators the need for pay restraint. I have asked for the briefing to cover this, and - assuming you agree - the draft reply refers to it.

R.

3 July 1979

2
PRIME MINISTER

Good news
MJS



Confederation of British Industry

21 Tothill Street
London SW1H 9LP
Telephone 01-930 6711
Telex 21332
Telegrams
Cobustry London SW1

From the Director-General: Sir John Methven

*We must write
and thank him
not*

GOV/PM/1

28 June 1979

Dear Prime Minister,

In the letter to you of 21 June, the President said that we would be writing to all CBI members urging them to respond to the new climate that you and your Government created by the Budget.

I now enclose a copy of the letter which I have just sent out. We shall be publicizing individual examples of actions taken by companies and management in the new climate. I have mentioned R T Z Wheal Jane in the letter to members and I also enclose a copy of the letter that I have had from Bob Thornton, Chief Executive of Debenhams, which arose from a conversation which I had with him and to which, I am sure that you will agree, he has responded in the fullest fashion.

We will also be publicizing shortly a note which should help managers to resist wage claims based on the RPI: and I will send that to you, if I may. I am sure that you will agree that it is absolutely essential that we all get over to the public in every possible way over the next two months the fact that people really will have more money in their pockets and that excessive wage claims pushed through by the unions, will, in the absence of much higher productivity, only lead to higher inflation and further loss of jobs. I hope that you will agree that we might discuss this information problem as one of the topics at the meeting on 9 July.

*Just say
John*

The Rt Hon Mrs Margaret Thatcher MP
Prime Minister
10 Downing Street
LONDON S W 1

Confederation of British Industry



From the Director General, Sir John Methven
To the Managing Director or Chief Executive

21 Tothill Street
London SW1H 9LP
Telephone 01-930 6711
Telex 21332
Telegrams
Cobistry London SW1

28 June 1979

Dear Member,

Over the last three years, I have written to all of you on a regular basis, explaining in my own words what I believe that the CBI had achieved and the objectives I thought we should be striking out for.

I had intended to use this letter as a normal report to you all. But that I now think would be wrong. This letter needs to be straightforward and to the point; and I would ask you all to read it and then discuss it with your colleagues throughout your organisation. My reason for asking this is as follows.

Every one of us knows that we are entering a crucial period in the UK. We have a Government which, in its Budget, has set out to do many of the things that on the personal incentives front we have so long argued for. They have taken risks, but they have been bold and courageous. They have been bold in dealing with the Price Commission. I believe too, that they intend to move firmly on the Industrial Relations front. If they don't, they will get pushed very sharply by the CBI!

So at last we have a Government which is intent on giving us - managers, employers and shopfloor - many of the conditions for which we have asked: and they are going to ask us all - as they are entitled to - how we are going to respond.

How can we - each of us - respond? At its meeting on Wednesday last week the CBI Council responded by passing the following resolution (and the CBI Council very rarely passes resolutions!):

'This Council fully supports the strategy and the direction of the Budget and recognises that its success will hinge to a large extent on the ability of managers and employers throughout business to respond to the challenge and the incentives it provides. The CBI Council therefore calls on all CBI member firms to do everything in their power through the efficient and competitive management of their enterprises to ensure that the policies, which the CBI has long advocated and which are now being pursued by the Government, lead to higher productivity, higher living standards, more jobs and a more successful economy, in the interests of the British people as a whole.'

The CBI, as I well know, has no power or right, of its own initiative, to make promises on behalf of its membership. It is not something I would ever attempt. But we have learned to act and fight together over the last three years when it

was really necessary - over Bullock, on Government contracts, on sanctions: and I thank you for that.

Now what I ask you to show on an individual and company basis is that you recognise that we have a new climate for business and that we can and will respond to it.

How? For example, by responding as RTZ did, when they decided to re-examine the possibility of acquiring and re-opening Wheal Jane, the tin-mine in Cornwall, without Government aid: by fighting to obtain moderation in wage levels in the coming months and above all by getting real productivity increases: by showing, publicly, by individual example after individual example, that we - as managers as employers - are responding to the new climate by specific actions on the investment front, on the wages and salaries front, on the productivity front and by explaining the facts of life to our work-force to a much greater extent than in the past - encouraging a much greater sense of involvement with the firm for which they work.

Those of you who are owners of independent small firms (and you comprise the vast majority of members of the CBI) have a special challenge. The way in which you respond to the encouragement of risk taking will be crucial to the success or failure of the Government's policy. I believe that now you have a real opportunity to do the job you should be doing - taking risks and creating prosperity as a result.

I do not pretend that the next 12 months, or even thereafter, will be easy. The world economic outlook is certainly difficult. Indeed it may be that the CBI will have substantial disagreements with the present Government, for example over what changes the Government should make in industrial relations legislation or over changes to competition policy. That is why the CBI is needed - to go on putting the business point of view, irrespective of who is in Government.

But that should not and, I believe, will not deter each and every one of us from responding to the new climate and doing our best (which means much better than in the past) to deliver a high output, high earnings economy which will enable us to create the free, prosperous and caring society in which we all believe.

If we fail in this new environment - when we are being given the sort of incentives we have asked for - we may never be believed again. We may never get such a chance again. And we shouldn't be surprised then if other, unpalatable, alternative strategies gain more attraction.

I can assure you that every one of the CBI staff in the Regions and in Tothill Street (not least myself) will be ready to help you. In particular I will be sending you shortly a note on inflation, pay and the changes in personal taxation which I hope that you will find helpful.

But please tell us specifically how you are responding to the new climate and what you are doing. We want to help to publicise it.

Yes, this is a call to arms. This is a call to be positive and to publicise what we are doing. This is a call to show that we believe in a market economy and that, when given the right conditions, we can make a market economy work for the benefit of the British people as a whole - even though it may take us some long time fully to succeed.

Yours sincerely,
John Pickens

Confederation of British Industry



From the Director-General: Sir John Methven

21 Tottill Street
London SW1H 9LP
Telephone 01-930 6711
Telex 21332
Telegrams
Cobustry London SW1

29 June 1979

Dear Sir,

Thank you very much indeed for your letter of 25 June 1979. If I may say so I was absolutely delighted to read it. I am taking the liberty of including a copy of your letter in a letter to the Prime Minister which I now enclose. I am sure that she will be as delighted as I am.

Are you going to publicise what you are doing? And, would it be possible for us to use the information provided that we do not in any way use your name unless you agree to it? I feel it is a question of getting a stone rolling: and what you have done should greatly help.

*Yours
Truly*

R C Thornton Esq
Deputy Chairman and Chief Executive
Debenhams Limited
1 Welbeck Street
London W1A 1DF

DEBENHAMS LIMITED

Telegrams: "DEBENHAM, LONDON, W.1"
Telephone: 01-550-4444
Telex: 281128

RC Thornton Ltd
LB

J Regyn

ONE WELBECK STREET,
LONDON, W1A 1DF

25th June, 1979

Sir John Methven,
Director General,
Confederation of British Industry,
21 Tothill Street,
London, SW1H 9LP.

25/6/79
21 Tothill St
London SW1H 9LP

Dear John,

I thought I would drop you a line and let you know something of the general feeling in the Debenham Group as a result of the new Budget.

First, and I am writing with restraint; there was a strong surge of patriotic feeling went through the senior management as the realisation sank in that here at last was a Government acting in the best interests of the country. With this came a determination to make the Budget work. Here are a few of the things we have decided to do as a result:-

1. The increase in V.A.T. has left us in some confusion about our sales, margins and stock planning for the future. The one point, however, which comes out most clearly is the grave danger of a drop in unit sales with resultant price increases throughout the Group. We have, therefore, as a matter of urgency, instituted a review of all our sources of supply to ensure that the axe falls most gently on the suppliers, particularly in the U.K., with whom we wish to have growing long term relations. This means, of course, a cruel blow to a number of fringe people; but we take the view that in any case one of our problems as a country is that we have too many fringe activities.
2. Although we regard ourselves as the lowest cost Department Store Group in the world, we have instituted another look at all our costs, particularly those associated with the bureaucracy, both our own and that of Whitehall which, as you know, imposes on us heavy demands for paper returns, etc. We are going to perform surgery with zest. I look forward to the first confrontation with some Whitehall Department asking /

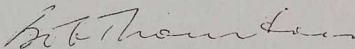
cont'd/

asking for returns that we are no longer going to send them. I should be glad if you would tell your friends in Government that this is going to happen and I will keep you informed of how the battle goes.

3. We have struggled here for a year or two with a number of fringe activities of our own and have probably been self-indulgent; we shall be closing down a number of these within a matter of weeks and hope to claw back £5m. of capital and put it to better use.
4. I am attaching an extract from the Financial Times of 15th June which gives you a clear picture of our investment programme and our optimism about the United Kingdom. It makes no mention there of the \$40m. of sales we achieve in the United States. We intend to grow in that market from profits achieved there and without cost to the U.K. will build up a hard selling, high return asset.
5. We believe that the Chancellor means what he says about credit and therefore we are increasing our credit charges in order to damp down this method of selling and, incidentally, make more money.
6. We are looking again at fuel and distribution costs and, in particular, at company motor cars. We hope to come up with an idea for putting the choice back on the individual. We provide over 700 company cars and what we have in mind is to give staff the money instead. We think this will encourage them to be more frugal in their use of cars and fuel.

It was a pleasure to see you again the other day and, on behalf of my colleagues I want you to be assured, and pass the message on, that we intend to support the Government in its actions.

Yours sincerely,



Debenhams begins to benefit from earlier developments

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F1

THE DEVELOPMENTS planned and started some years ago by Debenhams retail distributor are now coming on stream and the group is beginning to reap the benefits, says Sir Anthony Burney, the chairman.

As anticipated last year, the group opened two new stores during 1973 at Swansea and at Stockport. Both of these are showing good results and are coming fully up to directors' expectations.

In March this year, the group opened the first phase of the redevelopment of its Ipswich store and Sir Anthony says the whole new store should be in operation by autumn 1980.

Progress on the Blackburn store is on schedule and it is anticipated that it will be completed by the autumn of this year. Work on the new stores in Cardiff and Edinburgh is proceeding and these should be open in autumn next year.

Detailed plans for the major reconstruction of the group's Croydon property have now been completed and it will shortly be entering into negotiations for the financing of this new project.

As reported May 19, bad weather and industrial unrest early this year trimmed pre-tax profits from £28.26m to £23.31m for the year ended January 27, 1979, on sales, excluding VAT, of £99.14m (£94.93m). Trading profit after cost of finance rose by 39 per cent to £21.73m, but the effect of lost turnover in January was to reduce profit by £1.28m to £20.45m.

The directors are confident that trading profit in the current year will show a further substantial advance.

On a current cost basis, pre-tax profits are reduced to £17.8m against £21.2m last time, after adjustments for depreciation of £2.2m (same), self-financed cost

of sales £3.9m (£5.2m), less searing of £1.6m (£2.3m). The £74.83m surplus arising from a revaluation of the group's properties made in 1973, with retained profits, but less £3.3m written off goodwill, resulted in an increase in shareholders' funds from £170.75m to £246.45m. At balance date, total borrowings amounted to £74.6m, representing some 30 per cent of shareholders' funds, compared to around 31 per cent a year earlier.

Group fixed assets rose from £150.86m to £241.8m and net current assets were up from £71.92m to £52.41m.

29 JUN 1979



c.c. HMT

Economic Policy
JA



10 DOWNING STREET

THE PRIME MINISTER

25 June 1979

Dear Sir John,

Thank you for your letter of 21 June.

I was most gratified to see the excellent resolution which the CBI Council have approved on the Budget, and I greatly welcomed the fact that you will be writing to all your members asking them to respond positively. I am also grateful for your good wishes for my participation in the Tokyo Summit.

Yours sincerely
Margaret Thatcher

Sir John Hedley Greenborough, K.B.E.

CS

PRIME MINISTER

John Greenborough has now sent you a copy of the excellent CBI Resolution on the Budget, which Clive showed you on Wednesday. He also offers his good wishes for the Summit.

I attach a draft reply.

*A L K M Laver
(Duty Clerk)
PO The Lancaster*

22 June, 1979.



cc Mr Watson
Mr Hoskyns

BF A 3/79 JS

10 DOWNING STREET

From the Private Secretary

21 June 1979

copy on: ~~Comm. Int. P.C. 2 Strategy~~
Statistics June 1979. (S.O.) L. (Under)

The Prime Minister has expressed concern about the current provisions for corporate stock relief. Her impression is that it has a distorting influence on company behaviour in that companies tend to increase their stocks unnecessarily at the end of the financial year; and this also results in a loss to the Exchequer. I would be grateful if you could let me have comments on this point. It would be helpful if you could also let me know what are the Chancellor's plans for reviewing Corporation Tax generally: the Prime Minister has expressed the view that Corporation Tax has become an "optional tax", and she thinks that consideration should be given either to abolishing it altogether or to making it operative.

The Prime Minister has also asked what progress is being made in devising a "standard of living" index, which will include tax as part of the cost of living. She considers the creation of such an index to be very important in the context of future pay negotiations, and I should be glad if you would let me have a progress report.

This
B &
on
Strategy
file.

TPL

A.M.W. Battishill, Esq.,
HM Treasury.

Confederation of British Industry



From the President:

Sir John Hedley Greenborough KBE

21 Tothill Street
London SW1H 9LP
Telephone 01-930 6711
Telex 21332
Telegrams
Cobustry London SW1

21st June 1979

Mr Prime Minister,

drb

The CBI Council met yesterday for the first time since the Budget. A resolution was approved, of which I enclose a copy, and which expresses our strong support for the strategy and direction of the Budget, at the same time recognising and accepting the welcome opportunity and challenge it presents for employers and managers.

We will be writing to all our members asking for a vigorous response which is so essential to the achievement of an improved economy.

The Council also asked me to relay to you their hope that your participation in the Tokyo Summit Meeting will meet with great success. Whilst we are fully aware of the gravity of the international energy scene, we would hope that the meeting will continue the efforts of previous summits to bring about a sustainable rate of economic growth in the countries involved.

I am sending a copy of this letter to the Chancellor of the Exchequer.

Sincerely

John Greenborough

The Rt. Hon. Margaret Thatcher, MP,
Prime Minister,
10 Downing Street,
London, SW 1.

RESOLUTION APPROVED UNANIMOUSLY BY THE
CBI COUNCIL ON 20TH JUNE 1979

This Council fully supports the strategy and the direction of the Budget and recognises that its success will hinge to a large extent on the ability of managers and employers throughout business to respond to the challenge and the incentives it provides. The CBI Council therefore calls on all CBI member firms to do everything in their power through the efficient and competitive management of their enterprises to ensure that the policies, which the CBI has long advocated and which are now being pursued by the Government, lead to higher productivity, higher living standards, more jobs and a more successful economy, in the interests of the British people as a whole.

RECEIVED





10 DOWNING STREET

THE PRIME MINISTER

21 June 1979

Original in Cap R.
cc H.T. T
D.H.S.
I. G.W.
P.R.S.
T.P.L.
From Pat.

Dear Mr. Feld.

Thank you for your letter of 6 June.

You raised first of all the question of indirect tax increases. You will now have heard the precise details of our Budget proposals. We have carried out our Election pledges to reduce substantially the burden of income tax: our cuts overall (in addition to those enacted by the 'caretaker' Finance Act in April) total £2½ billion in 1979/80, and take an additional ¼ million people out of the tax net.

To pay for these cuts, we have always made it clear that we would have to increase indirect taxation. We have concentrated these increases on VAT. VAT is not a regressive tax: it covers about one half of consumers' expenditure and does not apply to necessities like food, children's clothing, domestic heating and lighting, public transport and housing.

The other major indirect tax increase was in the duties on hydro-carbon oil. Clearly, in view of the current difficulties in oil supplies, we could not leave these duties unchanged, but we did exclude paraffin, which is widely used by the less well-off for domestic heating, from the increase. The duty on petrol is in any case not particularly regressive: the table attached (which is being published in the June Supplement to the Treasury's Economic Progress Report) shows that the petrol and VAT increases together will form a lower proportion of their expenditure for

/ those on lower incomes.

those on lower incomes. The specific duties on alcoholic drinks and tobacco, which, taken as a whole, are regressive, we have left unchanged, even though their real value is falling with inflation.

I hope you will agree that so far from renegeing on our Election pledges our tax changes will not only improve the incentive to work and extend consumer choice as we promised, but have been formulated with their distributional effects very much in mind.

On pensions, I am sure that you were pleased when we announced the new rates which proved your fears about our intentions unfounded. The rates of £23.30 for a single person and £37.30 for a married couple from next November are higher than the rates you proposed on the basis of your pre-Budget arithmetic and, as such, should be doubly welcome to you.

These new rates take account of the shortfall in last November's pension rates and the expected increase in prices over the twelve months to November 1979. We have therefore much more than fulfilled the statutory requirements.

Yours sincerely
Margaret Thatcher

Frank Field, Esq., M.P.

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BUDGET SNAPSHOT, 12 JUNE 1979

This condensed summary gives some main points of the Chancellor's Budget proposals. Figures are in round terms. Those not in brackets relate to revenue in 1979/80, those in brackets to a full year, unless otherwise stated. Proposed changes needing legislation, including all tax changes are, of course, subject to Parliament's approval.

BUDGET AIMS

Entirely fresh approach needed to halt 25 years of Britain's economic decline. Poor performance due not to shortage of demand, but failures on "supply side" of economy. Failures not stopped, many caused, by Government interventions, laws and taxes stifling enterprise.

Strategy based on 4 principles

- (1) Strengthen financial incentives by allowing people to keep more of what they earn. Hard work will pay. Talent and ability will be rewarded.
- (2) Enlarge freedom of choice by reducing role of state and enlarging that of individuals.
- (3) Reduce burden of financing public sector to level leaving room for commerce and industry to prosper.
- (4) Ensure collective bargaining takes account of its consequences - encourage responsibility.

Complete change in way economy allowed to work. Motivate creation of genuine new jobs and of wealth, on which improvement of public services depends.

Budget changes are first step only in new direction, but take us a long way.

MAIN BUDGET SUMS (net)

	£bn 1979/80	Full year
Direct tax DOWN	3½ -	4½ -
Indirect Tax UP	2½	4½
Cash limits policy and public spending CUTS (1979 Survey Prices)	2½	-
Public assets to be SOLD	1	-

Results: Big switch from direct to indirect tax
Public Sector Borrowing Requirement (PSBR) for 1979/80 restricted to about £8½ bn (4½% of GDP) compared with £9¼m (5½% of GDP) last year.

NB: Pensioners, unemployed and others who may not benefit from direct tax cuts fully protected from price rises by November increase in benefits.

NET EFFECT OF TAX CHANGES - for next 10 months
(DIRECT AND INDIRECT)

Married couple - husband with job

Earnings per week:	£60	£100	£150
Income tax cuts	+£2.59	£4.07	£5.93
VAT and petrol duty	-£1.82	£2.76	£3.97
Net gain to pocket	77p	£1.31	£1.96

TAX MEASURES
PERSONAL TAXES

INCOME TAX - all changes backdated to 6 April.

PERSONAL ALLOWANCES all raised by over 18% from 1978/79

PEOPLE UNDER 65

Married (and single parent): UP £280 (from 1978/79) to £1,815

Single (and wife with job): UP £180 to £1,165

PEOPLE OVER 65 (AGE ALLOWANCE)

Married: UP £380 to £2,455 - Single: UP £240 to £1,540

Income ceiling: (to qualify for age allowance): UP £1,000 to £5,000 (25%)

Note: Increases in allowances are double those fixed, but not yet implemented, by the caretaker Finance Act in April. Age allowance ceiling raised £1,000 instead of £400.

New tax thresholds (per week):

UP from £29.52 to £34.90 (married) - UP from £18.94 to £22.40 (single).

Number taken out of tax altogether: 1.3 million.

About $\frac{1}{2}$ million more people will benefit from full age allowance.

COST: £1½bn (£2bn)

BASIC RATE

3p OFF. Down from 33p in £ to 30p

COST: £1½bn (£1½bn)

Aims: (of changes in allowances plus basic rate cut): Remove disincentive effects of heavy taxation on earnings at lower and middle levels. Allowances more than revalorised. Marginal rate on overtime etc cut. Ease problem of poverty trap.

Total tax cut (from personal allowances plus basic rate cut):

	<u>TAX CUT (£ a year)</u>			
	<u>Earnings per week</u>	<u>£60</u>	<u>£100</u>	<u>£150</u>
<u>Married</u> :		109.05	171.45	249.45
<u>Single</u> :		95.55	157.95	235.95

Rebates from personal allowance increases: generally payable from first pay day after 12 July or 26 July, according to coding.

Rebates from basic (and higher) rate tax cuts: payable after new tax tables reach employers in October.

LOWER RATE (25% on first £750 taxable income): NO CHANGE

HIGHER RATES

Threshold for 40% rate up from £8,000 to £10,000 (taxable income). Top rate down from 83% to 60%, payable at taxable income of £25,000. Bands widened. New structure:-

% tax	1979/80 £	1978/79 £
40	10,001 - 12,000	8,001 - 9,000
45	12,001 - 15,000	9,001 - 10,000
50	15,001 - 20,000	10,001 - 11,000
55	20,001 - 25,000	11,001 - 12,500
60	over 25,000	12,501 - 14,000
65		14,001 - 16,000
70		16,001 - 18,500
75		18,501 - 24,000
83		Over 24,000

Number taken out of higher rates: 550,000 out of potential 1.2 million.

Aims: Restore incentives to middle and senior managers. Help stop "brain drain". Add to value of differentials. Put top rate more in line with other industrial countries.

COST: £460m (£860m)

INVESTMENT INCOME SURCHARGE

NONE to be payable below single new threshold: £5,000 investment income. Single rate above that: 15%. (Replaces present two rates: 10% and 15% and 4 thresholds: £1,700 (10%) and £2,250 (15%) for under-65s and £2,500 and £3000 for over-65s).

The single threshold of £2,000 in 1973/74 would now be worth £4,650 in real terms. New threshold more than indexed.

Number relieved of surcharge altogether: about 550,000, including 250,000 people over 65, out of 850,000.

Note: Lower rate of 10% and special thresholds for over-65s introduced when main threshold cut to £1,000 by previous Government in 1974.

Aim: Encourage saving and provide funds for industry. Be fairer to those living on interest on savings from income already taxed.

COST: £22m (£200m)

WAR WIDOWS

War widows' pensions to be exempt from income tax altogether. At present half is taxable.

COST: £4m (£6m)

TAX RELIEF ON LOANS

Transitional relief on loans taken out before 26 March 1974 (eg on second homes) to be extended up to 5 April 1982 (instead of 1980). This gives Government time to consider rules on interest tax relief, particularly for investment in small companies

TOTAL INCOME TAX CUT IN REVENUE: £3½ bn (£4½bn)

TAXES ON SPENDING

VALUE ADDED TAX (VAT)

NEW SINGLE RATE OF 15%

from Monday, 18 June.

Present rates: Standard 8% on eg cars, clothes, pots and pans, furniture, drink and tobacco, meals out, sweets, services.

Higher 12½: on eg TV sets, washing machines, record players, jewellery, caravans, petrol, cameras, fur coats.

Zero rating of eg food, young children's clothes, gas electricity, housing, public transport, books, newspapers, medicines.

UNCHANGED.

Exemption of eg insurance, post, finance, health, funerals, unions: UNCHANGED

Price increases because of higher VAT:

Standard rated goods: about 6½% - Higher rated goods: about 2¼%.

Eg £15 pair of shoes: up 97p - £350 suite of furniture: up £22.69 - £200 washing machine: up £4.45 - £50 camera: up £1.11.

IMPACT ON RETAIL PRICES INDEX: +3½%

EXTRA REVENUE:

£2bn (£4½bn)

Aims: Help pay for direct tax cuts without raising prices of many necessities. Unified rate simplifies traders' tax work and costs. Gives 3-month once-for-all boost to companies' cash flow. Pensioners, unemployed etc protected!

Effective rate (across whole of consumers' spending) still only 8% (because of width of zero-rating and exemptions).

Note: 15% VAT will not apply to phone bills (held up by computer strike) for quarters starting before 1 November. Other transitional relief also.

DUTY ON OIL

PEIROL duty up 7p a gallon to about 37p from 6.00pm, 12 June.

With VAT change from 18 June, private motorists will pay about 10p more a gallon. Business users can claim back VAT.

EXTRA DUTY YIELD: £265m (£345m). Including VAT, petrol tax up £280m (£375m). IMPACT on RPI: 1½%

Aim: Encourage energy savings. Help shift to indirect tax.

Note: Before increase, duty in real terms down 40% since 1976.

DERV (diesel road fuel) duty: up 7p a gallon to nearly 42p (from 6pm 12 June).

Business users can deduct VAT.

Adds about 1p to road transport costs.

(EXTRA DUTY YIELD . £80m (£100m)

No extra cost to bus operators. Grants to them increased in line with duty.

HEAVY OIL (for industry)

Up ½p a gallon to 3p EXTRA DUTY YIELD: £40m (£50m)

Aim: industrial users should also help to conserve energy.

KEROSENE (paraffin and most central heating oil)

NO CHANGE (1p duty a gallon)

(Zero rated for VAT)

TOTAL EXTRA YIELD FROM OIL DUTIES (Inc Vat): £400m (£525m)

DRINK AND TOBACCO

VAT increase will add .6p to 20 cigarettes; about 2p to pint of beer (in pub); about 10p to bottle of table wine; about 25p to bottle of whisky. NO FURTHER CHANGES except technical change in cigarette duty.

CAR TAX NO CHANGE - 10%

VEHICLE EXCISE DUTY (VED) NO CHANGE - £50 on private car.

Government reviewing proposed switch from VED to petrol duty, and structure of lorry VED.

TOTAL INDIRECT TAX INCREASE:

£2½bn (£4½bn)

TAXES ON CAPITALCAPITAL GAINS TAX

NO CHANGE

CAPITAL TRANSFER TAX

NO CHANGE, EXCEPT: 2 year extension of transitional relief on distributions from discretionary trust. Government reviewing capital taxation.

BUSINESS TAXESPETROLEUM REVENUE TAX (PRT) -

PRT rate up from 45% to 60% from Jan-June tax period, plus other changes as proposed by previous Government. Two new changes in PRT expenditure rules.

BNOC no longer to be exempt from PRT. Increase in tax regime justified by recent oil price increase, to ensure fair public share. EXTRA TAX YIELD: £110m this yearEXTRA YIELD TO 1985: About £1.8 bn. (altogether).CORPORATION TAX - NO CHANGE IN RATES

(Main rate 52% - small company rate 42%)

SMALL COMPANIES' profits limit (for 42% rate) raised from £50,000 to £60,000.

Upper limit (where 52% applies) up from £85,000 to £100,000

COST: £6m (£11m)STOCK RELIEF

Relief outstanding for 1973/74 and 1974/75 to be written off. Relief for later years to be written off after six years. Other help, particularly for small firms.

COST: NIL (£55m)ADVANCE CORPORATION TAXRate down from 33/67 to 30/70, in line with basic rate of income tax. No full year cost, as mainstream corporation tax increased accordingly.FIRST YEAR COST £190mSUB-CONTRACTORS (Building Industry)

Deduction rate cut to 30% in line with basic rate, from 6 November.

BUSINESS CAR LEASINGTAX LOOPHOLE CLOSED From 12 June, leased cars to qualify for 25% capital allowance per year, like other business cars. (At present, in practice, 100% in first year).

Limit for higher-priced cars raised to £2,000 (£1,250) for cars costing over £8,000 (£5,000).

SAVING OF TAX LOSS: £200m (full year)DEVELOPMENT LAND TAX

NEW SINGLE RATE OF 60% on disposals over £50,000 per year. (At present £10,000 exempt, next £50,000 at 73%, over that 80%).

Aim: simplify, and restore market in land for development.COST: £2m (£10m)

MONETARY MEASURES

Progressive reduction of TARGET RANGE for growth of MONEY SUPPLY. Present range of 8-12% growth of Sterling M3 for year to mid-October 1979 to be lowered to: 7-11% annual rate for period mid-June 1979 to mid-April 1980.

MINIMUM LENDING RATE increased by 2 per cent to 14 per cent

CORSET (Supplementary Special Deposits Scheme). Squeeze to be continued for further 3 months to mid-December.

Aims: keep firm grip on financial conditions, restrain inflation, encourage responsible pay bargaining, assist exchange rate stability.

Note: Public spending cuts make it possible to hit lower money targets with less restraint on private sector.

DIVIDEND CONTROL ENDS from 1 August. Present law limiting most annual dividend increases to 10% expires 31 July. WILL NOT BE RENEWED.

Aims: Stop distortion of markets. Ease flow of funds for industry. Help retired people. Administrative savings. Counterpart of free pay bargaining and price policy based on competition.

EXCHANGE CONTROL

Companies £5m a year can be invested abroad in each new project, without paying dollar premium.

All overseas earnings can be reinvested abroad.

Merchants again able to finance 3rd-country trade in sterling.

Families £100,000 each per year for buying property abroad, without paying dollar premium. Emigrants can take £200,000 abroad. Annual limit on cash gifts goes up to £10,000 per donor. £1,000 a trip for foreign travel instead of £500. Easier terms for buying foreign shares.

Aim: End distortions. Help smaller firms' investment abroad. Strengthen demand for UK exports. Cut administrative costs. Discussed with EEC Commission.

SPENDING MEASURES

Main sums for 1979/80

£bn 1979 Survey prices*

Cash limits squeeze

1

Cuts in spending

1½

* Autumn 1978 for goods and services. Nationalised industries: average 1978/79 prices. Some other prices: estimated average 1979/80.

CASH LIMITS, 1979/80

No increase to allow for extra price rises (as laid down by previous Government).

Civil Service limits cut by 3% before allowing for extra pay rises. Rate Support Grant for Local Authorities cut by £335m after allowing for Government's share of cost of extra pay rises. Final decision on amount of cuts, when further pay rises known. Up to local authorities to decide on savings.

Note: Cash limits apply a ceiling to spending even if pay and/or prices rise more than expected. Volume of service, number of staff etc, may have to be cut if that happens.

Nationalised industries - see below.

SPECIFIC SPENDING CUTS1. E. AND

£m at 1979 Survey prices

ENVIRONMENT

Housing: £300m. Mainly local authority investment. Enough left to cover forecast housebuilding approvals and vigorous improvement programme.
Water: £55m. Community Land Act repeal: £50m. Other: £32m.

437

INDUSTRY

4-month deferment of Regional Development Grant payments: £145m.
DoI and MEB spending: £55m. Savings by Post Office and British Aerospace: £10m.

210

ENERGY

Saving in finance for ENOC: £45m, electricity: £82m, gas: £171m, and coal industries: £25m. Asked to avoid price increases more than needed by previous Government's cash limits.

323

EMPLOYMENT

Cuts in MSC and DE employment and training programmes. Designed to concentrate help where most needed. Tax cuts better than subsidies in creating real jobs.

172

EDUCATION & SCIENCE

No pilot scheme for 16-18 mandatory grants: £10m, cuts in building: £14m, university etc grants: £9m, science budget: £5m, overseas students' fees: £6m. Other: £11½m.

55½

ARTS, LIBRARIES, HERITAGE

Arts, libraries: £3m, National Land Fund: £1½m.

4½

HEALTH

No cuts in Health Service. Prescription charges up from 20p to 45p. Unchanged since 1971. Less than indexed by RPI. Continued exemption of children, old people, etc. Certain dental charges also up. Extra Revenue (Gt. Britain)

34

AID

Cut to £790m. Aid total still higher than in 1978/79 in real terms.

50

TRADE

Price Commission and other savings: £5m. Co-op Bank to refinance export credit: £25m.

30

TRANSPORT

BR cash limit cut: £14m. Rail freight grants: £1m. Trunk road spending: £10m. Will not mean deferring top priority schemes.

25

£m at 1979 Survey prices

2. SCOTLAND

Not including Scotland's share of prescription charges 76

3. WALES Not including Wales's share of prescription charges and education. 164. N. IRELAND 35

Note: Where the Secretaries of State for Scotland, Wales and Northern Ireland have separate responsibilities for some of above programmes, comparable reductions will be made.

TOTAL SPECIFIC SPENDING CUTS £1.468bnCONTINGENCY RESERVE CUT £250m

Just over £250m remains for unforeseen extra spending.

DEFENCE

Additional spending, mainly on equipment £100m

General points

Cuts first step in shifting balance from public spending and making room for tax cuts. Consumers not Government to decide own spending. Finance to determine expenditure, not vice versa. Cuts in capital spending kept to minimum possible.

SALE OF PUBLIC ASSETS

SALES to private sector in 1979/80: £1bn.

Will help cut PSBR, widen participation in ownership of industry. Biggest contribution this year: sale of BP shares.

TOTAL SAVINGS FROM SPENDING CUTS AND ASSET SALES: £3.1bn (1979 Survey prices)
£4 bn (current prices)

SOCIAL SECURITYRETIREMENT PENSIONS: Up in November

Married: UP £6.10 to £37.30 - Single: UP £3.80 to £23.30

Increases (almost 20%) take full account of expected price rises after VAT increase, plus last year's undershoot.

Christmas bonus: £10 per pensioner. Pensions to be price protected in future.

CHILD BENEFIT: NO CHANGE, but for working lone parents, child benefit premium

UP from £2 to £2.50 in November.

Mobility Allowance (for severely disabled).

UP from £10 to £12 in autumn.

UNEMPLOYMENT AND OTHER BENEFITS

Increases to be announced tomorrow.

Confederation of British Industry



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Cobustry London SW1

From the Director-General: Sir John Methven

Prime Minister

The CBI Council passed the attached resolution this afternoon.

When I saw John Methven 20 June 1979
today, he made it clear that he has got the
message that Ministers are now expecting action
from the CBI and its members.

Dear Chris,

JSM: 20/6

As promised, I attach a

copy of the Resolution passed by the CBI

Council 15-6-79. I am writing to all
members urging them to act on the
resolution and to spell out their
views there.

Yours sincerely,

John Methven

This Council fully supports the strategy and the direction of the Budget and recognises that its success will hinge to a large extent on the ability of managers and employers throughout business to respond to the challenge and the incentives it provides. The CBI Council therefore calls on all CBI member firms to do everything in their power through the efficient and competitive management of their enterprises to ensure that the policies, which the CBI has long advocated and which are now being pursued by the Government, lead to higher productivity, higher living standards, more jobs and a more successful economy, in the interests of the British people as a whole.

Passed by the CBI Council 20/6/79

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10 DOWNING STREET

THE PRIME MINISTER

18 June 1979

Dear Mr. Ivens

Thank you for your letter of 14 June.
As you say, the Chancellor's Budget fulfils our Election promises, and I am sure the vast majority of people in the country welcome it. It is now for everyone to grasp the new opportunities which the Budget provides, so that we can achieve a real turn-around in our economic fortunes.

Yours sincerely

MT

Michael Ivens, Esq.

jfh

CAZENOVE & CO.

cc Sue Goodchild

Box

12 Tokenhouse Yard
London EC2R 7AN

L. HEINERTZHAGEN

J. R. HENDERSON	F. B. MITFORD-SLADE
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LORD PARKINGDON	A. H. J. MUIR
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D. L. MATHEW	B. E. A. PASCOE

TELEPHONE: 01-588 3828

MJdeRR/FS

13th June, 1979

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Dear Margaret.

It was very kind of you to ask Paddy and I to lunch today in honour of the President of Kenya. We both enjoyed it very much and it was particularly nice to see you for the first time as Prime Minister and at 10, Downing Street.

I thought, perhaps, that I should just emphasise the remarks that I made to you about the Budget. I had a long talk with Ian Gow during lunch and told him of our views in detail, but in principle it was exactly the Budget that we, and the vast majority of the people in the City, were hoping for. We believe it gives industry and the City the opportunity to rebuild the country's financial strength which will, in the end, enable us to hold up our heads again in this competitive world. The short term reaction in the market is to mark both Gilts and equities down. This is only a symptom of the difficulties we know we all have to face, probably in the autumn, but we are certain that once industry has overcome these temporary difficulties the future will look more secure and the market will reflect these hopes.

Please lean on us if there is anything we can do to help.

James Evers
Michael

The Rt. Hon. Mrs. Margaret Thatcher, MP.,
Prime Minister,
House of Common,
London S.W.1.



H. M. TREASURY

Parliament Street, London SW1P 3AG, Press Office: 01-233-3415
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R
12 June 1979

1979 BUDGET EXPLANATORY TABLES

The Income Tax Proposals

The Chancellor's main income tax proposals are as follows:

- Increases in the main personal allowances of over 18 per cent compared with 1978-79. These increases are double those contained in the pre-Election Caretaker Finance Act. The proposed increases are:

	1978-79 level £	Proposed increase £	1979-80 proposed level £
Single person's allowance (and wife's earned income relief)	985	180	1165
Married man's allowance	1535	280	1815
Age allowance (single)	1300	240	1540
Age allowance (married)	2075	380	2455
Additional personal allowance	550	100	650

- A 3p cut in basic rate from 33 per cent to 30 per cent.
- A cut from 83 per cent to 60 per cent in the top rate of income tax.
- A raising of the point (from £8000 to £10000) at which higher rate tax starts to be paid; and a stretching out of the higher rate bands.

The new structure of tax rates will be:

Rate of tax	1979-80 taxable income	1978-79 taxable income
£	£	£
25	0- 750	0- 750
30	751-10,000	
33		751- 8,000
40	10,001-12,000	8,001- 9,000
45	12,001-15,000	9,001-10,000
50	15,001-20,000	10,001-11,000
55	20,001-25,000	11,001-12,500
60	over 25,000	12,501-14,000
65		14,001-16,000
70		16,001-18,500
75		18,501-24,000
83		over 24,000

- An increase in the threshold for the investment income surcharge to £5000 for all taxpayers. This doubles the threshold for those aged 65 or over and more than doubles it for those under 65. The 10 per cent rate of surcharge is to be abolished.
- An increase in the age allowance income limit from £4000 (in 1978-79) to £5000.

The Indirect Tax Proposals

The Chancellor's main indirect tax proposals are:

- Unification of the standard and higher rates of VAT at 15 per cent.
- Increases of around 7p a gallon in petrol and derv duties, and $\frac{1}{2}$ p a gallon in rebated oil duty (excluding burning oil and paraffin).

Vat in this country covers about half of consumer expenditure. It does not apply to necessities like food, children's clothing, domestic heating and lighting, public transport or housing. In general these items tend to account for a larger proportion of total expenditure at lower than at higher income levels. Unification at 15 per cent means, therefore, that the average effective rate of VAT on total consumer spending will be about 8 per cent. Up-to-date comparable figures for other EEC countries are not available. They depend on the changing pattern of consumption as well as the latest structure of VAT rates. The most recent comparative figures (1976) suggest that the new UK effective rate will be amongst the lowest in the Community. The figures for many other EEC countries are in the range of 11 to 15 per cent.

Petrol taxation has been falling sharply in real terms in the last few years. Between February 1974 and April 1979, a period in which the RPI increased by 110 per cent, petrol taxation rose by only 78 per cent. And the share of taxation in the total price of petrol has fallen from over 60 per cent in the spring of 1973 before the oil price rise to less than 43 per cent immediately before the Budget. It will now be about 48 per cent, assuming a price after the Budget of around £1.05 a gallon.

Timing of Changes

The changes in the duties on petrol, derv and rebated oil will take effect from 6pm today. The unification of VAT will take effect from Monday 18 June.

The increases in the personal allowances (including refunds of tax overpaid since 6 April) should be reflected in pay packets for the bulk of those on PAYE on the first pay day after 12 July. The cut in basic rate and the reductions in higher rate tax (again with refunds) should affect pay packets from the first pay day after 5 October.

The Effects of the Changes

The substantial cuts in income tax are the keystone of the Chancellor's policy. They are designed to improve incentives by giving greater rewards for hard work, responsibility and success. Those at the bottom of the earnings ladder should benefit in particular from the increases in the personal allowances. Those in the middle will benefit from the cut in basic rate. And the higher rate taxpayer will benefit in particular from the reduction in the present high marginal rates.

The Chancellor explained in his Budget Speech that the cuts in income tax are only the first instalment of changes to come.

The increases in the personal allowances mean that no tax at all will be paid by some 1.3 million people who would have been liable had the allowances remained at 1978-79 levels; over 700,000 of these would have been liable if the allowances had remained at the level fixed in the Caretaker Finance Act. The increases in the higher rate threshold will mean that there will be some 450,000 fewer higher rate taxpayers than would otherwise have been the case.

The loss of revenue because of the cuts in income tax will be some £3.5 billion in 1979-80 and some £4.5 billion in a full year.

The room for the cuts in income tax has come from a combination of reductions in public expenditure and increases in VAT and the duties on petrol, derv and rebated oil. The indirect tax changes taken together will raise about £2.4 billion in 1979-80 and £4.7 billion in a full year. The direct impact on the RPI will be about $3\frac{1}{2}$ per cent.

The switch from taxes on income to taxes on spending will substantially increase the freedom of wage and salary earners - those who produce our goods and services - to do with their money what they, and not the Government, think best.

As the Chancellor pointed out in his Budget Speech, the income tax reductions will be retrospective to April 1979, so the benefit of a full year's tax cuts will be concentrated into the next ten months. Over this period, the increase in net take home pay arising from the reductions in income tax will more than make up for the rise in prices associated with the changes in VAT and oil duties.

The Explanatory Tables

The attached tables 1 to 6 show the effects, compared with 1978-79, of the changes in income tax proposed in the Budget on single and married taxpayers at different levels of income for the 1979-80 financial year as a whole. There are separate tables for elderly persons benefiting from the increases in the age allowances and the age allowance income limit, as well as from the changes in the investment income surcharge. Tables 5 and 6 give the information in the form of weekly instead of annual incomes at levels up to £200 a week, averaged over the whole year.

Table 7 shows the weekly net income of a family with two young children in 1979-80, compared with 1978-79, after taking account of the increases in Child Benefit and National Insurance contributions.

Tables 8 and 9 show how, for single people and married couples, the income tax burden - the proportion of income taken in income tax - has varied between 1973-74 and 1979-80. (The comparative income levels have been arrived at by reference to the retail prices index.)

PRESS OFFICE
H M TREASURY
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94/79

SINGLE PERSONS - INCOME ALL EARNED - ANNUAL FIGURES

TABLE 1

Income	Charge for 1978/79		Proposed charge for 1979/80		Reduction in tax after proposed changes
	Income tax	Percentage of total income taken in tax	Income tax	Percentage of total income taken in tax	
£	£	per cent	£	per cent	£
1,500	129	8.6	84	5.6	45
2,000	275	13.8	213	10.7	62
2,500	440	17.6	363	14.5	77
3,000	605	20.2	513	17.1	92
3,500	770	22.0	663	18.9	107
4,000	935	23.4	813	20.3	122
4,500	1,100	24.4	963	21.4	137
5,000	1,265	25.3	1,113	22.3	152
6,000	1,595	26.6	1,413	23.6	182
7,000	1,925	27.5	1,713	24.5	212
8,000	2,255	28.2	2,013	25.2	242
9,000	2,586	28.7	2,313	25.7	273
10,000	2,987	29.9	2,613	26.1	374
15,000	5,664	37.8	4,588	30.6	1,076
20,000	9,091	45.5	7,030	35.2	2,061
25,000	12,843	51.4	9,722	38.9	3,121
30,000	16,992	56.6	12,663	42.2	4,329

TABLE 2

MARRIED COUPLES - INCOME ALL EARNED - ANNUAL FIGURES

Income	Charge for 1978/79		Proposed charge for 1979/80		Reduction in tax after proposed changes
	Income tax	Percentage of total income taken in tax	Income tax	Percentage of total income taken in tax	
£	£	per cent	£	per cent	£
2,000	116	5.8	46	2.3	70
2,500	258	10.3	171	6.9	87
3,000	423	14.1	318	10.6	105
3,500	588	16.8	468	13.4	120
4,000	753	18.8	618	15.5	135
4,500	918	20.4	768	17.1	150
5,000	1,083	21.7	918	18.4	165
6,000	1,413	23.6	1,218	20.3	195
7,000	1,743	24.9	1,518	21.7	225
8,000	2,073	25.9	1,818	22.7	255
9,000	2,403	26.7	2,118	23.5	285
10,000	2,766	27.7	2,418	24.2	348
15,000	5,334	35.6	4,296	28.6	1,038
20,000	8,680	43.4	6,705	33.5	1,975
25,000	12,428	49.7	9,364	37.5	3,064
30,000	16,535	55.1	12,273	40.9	4,262

ELDERLY SINGLE PERSONS (AGED 65 OR OVER) - ANNUAL FIGURES

TABLE 3

Income	Charge for 1978/79		Proposed charge for 1979/80		Reduction in tax after proposed changes
	Income tax	Percentage of total income taken in tax	Income tax	Percentage of total income taken in tax	
£	£	per cent	£	per cent	£
Income all earned					
2,000	175	8.8	115	5.8	60
2,500	335	13.4	250	10.0	85
3,000	500	16.7	400	13.4	100
3,500	665	19.0	550	15.7	115
4,000	830	20.8	700	17.5	130
4,500	1,100	24.4	850	18.9	250
5,000	1,265	25.3	1,000	20.0	265
5,500	1,429	26.0	1,250	22.7	179
6,000	1,595	26.6	1,413	23.6	182
7,000	1,925	27.5	1,713	24.5	212
8,000	2,255	28.2	2,013	25.2	242
9,000	2,586	28.7	2,313	25.7	273
10,000	2,987	29.9	2,613	26.1	374
Income half earned, half from investments					
Up to £5,000 as above					
5,500	1,454	26.5	1,250	22.7	204
6,000	1,645	27.4	1,413	23.6	232
7,000	2,050	29.3	1,713	24.5	337
8,000	2,455	30.7	2,013	25.2	442
9,000	2,861	31.8	2,313	25.7	548
10,000	3,337	33.4	2,613	26.1	724

TABLE 4

ELDERLY MARRIED COUPLES (EITHER HUSBAND OR WIFE AGED 65 OR OVER) - ANNUAL FIGURES

Income	Charge for 1978/79		Proposed charge for 1979/80		Reduction in tax after proposed changes
	Income tax	Percentage of total income taken in tax	Income tax	Percentage of total income taken in tax	
£	£	per cent	£	per cent	£
Income all earned					
2,500	106	4.3	11	0.5	95
3,000	245	8.2	136	4.5	109
3,500	410	11.7	276	7.9	134
4,000	575	14.4	426	10.7	149
4,500	850	18.9	576	12.8	274
5,000	1,083	21.7	726	14.5	357
5,500	1,248	22.7	976	17.7	272
6,000	1,413	23.6	1,218	20.3	195
7,000	1,743	24.9	1,518	21.7	225
8,000	2,073	25.9	1,818	22.7	255
9,000	2,403	26.7	2,118	23.5	285
10,000	2,766	27.7	2,418	24.2	348
Income half earned, half from investments					
Up to £5,000 as above					
5,500	1,273	23.2	976	17.7	297
6,000	1,463	24.4	1,218	20.3	245
7,000	1,868	26.7	1,518	21.7	350
8,000	2,273	28.4	1,818	22.7	455
9,000	2,678	29.8	2,118	23.5	560
10,000	3,116	31.2	2,418	24.2	698

TABLE 9

SINGLE AND MARRIED COUPLES - INCOME ALL EARNED - WEEKLY FIGURES

Income	Charge for 1978/79		Proposed charge for 1979/80		Reduction in tax after proposed changes
	Income tax	Percentage of total income taken in tax	Income tax	Percentage of total income taken in tax	
£	£	per cent	£	per cent	£
	Single persons				
30.00	2.77	9.2	1.90	6.3	0.87
35.00	4.15	11.8	3.15	9.0	1.00
40.00	5.80	14.5	4.56	11.4	1.24
50.00	9.10	18.2	7.56	15.1	1.54
60.00	12.40	20.7	10.56	17.6	1.84
70.00	15.70	22.4	13.56	19.4	2.14
80.00	19.00	23.7	16.56	20.7	2.44
90.00	22.30	24.8	19.56	21.7	2.74
100.00	25.60	25.6	22.56	22.6	3.04
120.00	32.20	26.8	28.56	23.8	3.64
150.00	42.10	28.1	37.56	25.0	4.54
200.00	60.90	30.5	52.56	26.3	8.34
	Married Couples				
35.00	1.37	3.9	0.02	0.1	1.35
40.00	2.62	6.6	1.27	3.2	1.35
50.00	5.61	11.2	3.81	7.6	1.80
60.00	8.91	14.8	6.81	11.3	2.10
70.00	12.21	17.4	9.81	14.0	2.40
80.00	15.51	19.4	12.81	16.0	2.70
90.00	18.81	20.9	15.81	17.6	3.00
100.00	22.11	22.1	18.81	18.8	3.30
120.00	28.71	23.9	24.81	20.7	3.90
150.00	38.61	25.7	33.81	22.5	4.80
200.00	56.27	28.1	48.81	24.4	7.46

ELDERLY SINGLE AND MARRIED COUPLES - INCOME ALL EARNED - WEEKLY FIGURES

TABLE 6

Income	Charge for 1978/79		Proposed charge for 1979/80		Reduction in tax after proposed changes
	Income tax	Percentage of total income taken in tax	Income tax	Percentage of total income taken in tax	
£	£	per cent	£	per cent	£
	Elderly Single persons				
30.00	1.25	4.2	0.10	0.3	1.15
35.00	2.50	7.1	1.35	3.8	1.15
40.00	3.80	9.5	2.60	6.5	1.20
50.00	7.09	14.2	5.39	10.8	1.70
60.00	10.39	17.3	8.39	14.0	2.00
70.00	13.69	19.6	11.39	16.3	2.30
80.00	17.67	22.1	14.39	18.0	3.28
90.00	22.29	24.8	17.39	19.3	4.90
100.00	25.59	25.6	21.16	21.2	4.43
120.00	32.20	26.8	28.56	23.8	3.64
150.00	42.10	28.1	37.56	25.0	4.54
200.00	60.90	30.5	52.56	26.3	8.34
	Elderly Married Couples				
50.00	2.53	5.0	0.70	1.4	1.83
60.00	5.48	9.1	3.20	5.3	2.28
70.00	8.78	12.5	6.12	8.7	2.66
80.00	12.76	15.9	9.12	11.4	3.64
90.00	18.26	20.3	12.12	13.5	6.14
100.00	22.10	22.1	15.88	15.9	6.22
120.00	28.71	23.9	24.81	20.7	3.90
150.00	38.61	25.7	33.81	22.5	4.80
200.00	56.27	28.1	48.81	24.4	7.46

TABLE 7

FAMILIES WITH CHILDREN
MARRIED COUPLE WITH 2 CHILDREN NOT OVER 11 - NET WEEKLY INCOME

Weekly earnings	Net weekly income in 1978/79 (after November 1978 increase in child benefit) (See Note)				Net weekly income in 1979/80 including proposed tax changes				Increase in net income
	Child benefit	Income tax	National insurance contributions	Net income	Child benefit	Income tax	National insurance contributions	Net income	
£	£	£	£	£	£	£	£	£	£
35.00	6.00	0.41	2.27	38.32	8.00	0.02	2.27	40.71	2.39
40.00	6.00	1.66	2.60	41.74	8.00	1.27	2.60	44.13	2.39
50.00	6.00	4.33	3.25	48.42	8.00	3.81	3.25	50.94	2.52
60.00	6.00	7.63	3.90	54.47	8.00	6.81	3.90	57.29	2.82
70.00	6.00	10.93	4.55	60.52	8.00	9.81	4.55	63.64	3.12
80.00	6.00	14.23	5.20	66.57	8.00	12.81	5.20	69.99	3.42
90.00	6.00	17.53	5.85	72.62	8.00	15.81	5.85	76.34	3.72
100.00	6.00	20.83	6.50	78.67	8.00	18.81	6.50	82.69	4.02
120.00	6.00	27.43	7.80	90.77	8.00	24.81	7.80	95.39	4.62
150.00	6.00	37.33	7.80	110.87	8.00	33.81	8.77	115.42	4.55
200.00	6.00	54.73	7.80	143.47	8.00	48.81	8.77	150.42	6.95

Notes

Net income is earnings, less tax and national insurance contributions, plus child benefit. It does not include any means-tested benefit.

National insurance contributions are for a person not contracted out of the new pension scheme.

Child Benefit was increased from £2.30 to £3.00 a week for each child in November 1978.

TABLE 8

SINGLE PERSON - INCOME ALL EARNED - COMPARISON WITH 1973/74

Income in 1979/80	Proposed charge for 1979/80		Equivalent gross income in 1973/74	Tax charged in 1973/74		Change in the percentage of income taken in tax (Column A minus column B)
	Income tax	Percentage of total income taken in tax (A)		Income tax	Percentage of gross income taken in tax (B)	
£	£	per cent	£	£	per cent	per cent
1,500	84	5.6	645	15	2.3	3.3
2,000	213	10.7	860	79	9.2	1.5
2,500	363	14.5	1,075	144	13.4	1.1
3,000	513	17.1	1,290	208	16.2	0.9
3,500	663	18.9	1,505	273	18.1	0.8
4,000	813	20.3	1,720	337	19.6	0.7
4,500	963	21.4	1,935	402	20.8	0.6
5,000	1,113	22.3	2,151	467	21.7	0.6
6,000	1,413	23.6	2,581	596	23.1	0.5
7,000	1,713	24.5	3,011	725	24.1	0.4
8,000	2,013	25.2	3,441	854	24.8	0.4
9,000	2,313	25.7	3,871	983	25.4	0.3
10,000	2,613	26.1	4,301	1,112	25.9	0.2
15,000	4,588	30.6	6,452	1,843	28.6	2.0
20,000	7,030	35.2	8,602	2,854	33.2	2.0
25,000	9,722	38.9	10,753	4,045	37.6	1.3
30,000	12,663	42.2	12,903	5,350	41.5	0.7

The equivalent gross income in 1973/74 is obtained by dividing the 1979/80 income by 2.325, the factor by which prices (measured by the retail prices index) have increased between April 1973 and April 1979.

TABLE 9

MARRIED COUPLES - INCOME ALL EARNED - COMPARISON WITH 1973/74

Income in 1979/80	Proposed charge for 1979/80		Equivalent gross income in 1973/74	Tax charged in 1973/74		Change in the percentage of income taken in tax (Column A minus column B)
	Income tax	Percentage of total income taken in tax (A)		Income tax	Percentage of gross income taken in tax (B)	
£	£	per cent	£	£	per cent	per cent
2,000	46	2.3	860	25	3.0	-0.7
2,500	171	6.9	1,075	90	8.4	-1.5
3,000	318	10.6	1,290	154	12.0	-1.4
3,500	468	13.4	1,505	219	14.6	-1.2
4,000	618	15.5	1,720	283	16.5	-1.0
4,500	768	17.1	1,935	348	18.0	-0.9
5,000	918	18.4	2,151	413	19.2	-0.8
6,000	1,218	20.3	2,581	542	21.0	-0.7
7,000	1,518	21.7	3,011	671	22.3	-0.6
8,000	1,818	22.7	3,441	800	23.2	-0.5
9,000	2,118	23.5	3,871	929	24.0	-0.5
10,000	2,418	24.2	4,301	1,058	24.6	-0.4
15,000	4,296	28.6	6,452	1,771	27.5	1.1
20,000	6,705	33.5	8,602	2,763	32.1	1.4
25,000	9,364	37.5	10,753	3,938	36.6	0.9
30,000	12,273	40.9	12,903	5,233	40.6	0.3

The equivalent gross income in 1973/74 is obtained by dividing the 1979/80 income by 2.325, the factor by which prices (measured by the retail prices index) have increased between April 1973 and April 1979.



with compliments

J B UNWIN

Treasury Chambers
Parliament Street
London SW1P 3AG

Tel: Direct Line 01-233

Switchboard 01-233-3000

By Minister

Fin

Please regard as a
Your Ref query for
your own guidance
only. I have
not given
my own
attention to it
yet, but intend
to put a note
downing on
this to Green
tomorrow. 13/vi

DRAFT PASSAGE FOR SPEECH

Budget - Economic
file Policy

We hear a lot about the low paid. It is a good political phrase, because it has immediate appeal to the sympathy of most of us. As the Rt Hon Member for Leeds East knows well enough, it is often used in pay negotiations by the union side to justify jacking up the whole of a pay structure : appeal first to sympathy for the low paid, then to reason to maintain differentials.

But what does the phrase really cover? In its report on low incomes the Royal Commission on the Distribution of Income and Wealth decided to use as a rough benchmark for their analysis earnings below the level of the lowest decile for full-time manual men : this broadly covered the lowest 25 per cent of income recipients. The Royal Commission found that this group consisted of 7 million family units, grouped in 5 million households and containing some 13 million people of all ages. 60 per cent of these families have no earnings and are almost wholly dependent on state benefits. The Commission found that there is considerable mobility of individuals and groups into and out of their lower incomes category.

We must also take into account the fact that most low earners in employment are either juveniles or women, many of them working part-time, who are not the principal breadwinners in a family.

The Rt Hon Member for Cardiff South-East said the other day that the Budget did nothing for the low paid who do not pay tax. The first thing I must point out to him is that the additional increase in the tax threshold over the statutory increase in the caretaker Finance Act has removed a further 700,000 people from tax altogether : the two increases together remove 1,300,000 people. I am sure they would tell the Rt Hon Member that the Budget has certainly done something for them.

But as regards those already out of tax before the caretaker Finance Act, on the basis of the Royal Commission figures some 60 per cent of them will be covered by the increases in state benefits we have announced as part of our Budget package.

The remainder, those in employment, must in general have been earning about £30 to £40 a week if they were married or less than £20 a week if they were single if they escaped tax in the last financial year. There cannot be many such people who are also principal breadwinners. The 1978 New Earnings Survey indicated that there were only about 100,000 adult men in full-time employment earning less than £40 a week in April 1978, and only 30,000 earning less than £30. The numbers are surely smaller today. Depending on their family circumstances, breadwinners in this small group may be entitled to Family Income Supplement, which we have announced we are uprating by 17½ per cent.

The Budget has thus helped the great majority of the low paid directly. But more important, it provides the incentives and climate of opportunity which we believe will inspire all the British people to work harder and produce more, thus sharing in the economic benefits which we are convinced will result from the opportunities that we have created.

BUDGET - SECRET



10 DOWNING STREET

From the Private Secretary

12 June 1979

Dear Mr. Hunt,

RATE SUPPORT GRANT 1979-80

The Prime Minister has considered the Chancellor of the Exchequer's minute of 7 June; in the light of your letter of 11 June explaining the breakdown as between Scotland and England and Wales of the RSG reduction, she is content with the Chancellor's proposals - including the draft paragraph in his Budget Speech.

I am sending copies of this letter to the Private Secretaries to the Home Secretary, the Secretaries of State for the Environment, Education, Social Services, Scotland, Wales and Transport and to Sir John Hunt.

Yours etc.

T. M. Hunt

M.A. Hall, Esq.,
H.M. Treasury.

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Published Papers

The following published paper(s) enclosed on this file have been removed and destroyed. Copies may be found elsewhere in The National Archives.

House of Commons Hansard
Budget Statement

12 June 1979
Columns 235-308

Financial Statement and Budget Report 1979-80
HMSO 12 June 1979

Signed AWayland Date 9 March 2010

PREM Records Team

Cabinet / Cabinet Committee Document

The following document, which was enclosed on this file, has been removed and destroyed. Such documents are the responsibility of the Cabinet Office. When released they are available in the appropriate CAB (CABINET OFFICE) CLASSES.

Reference: CC(79) 5th Conclusions

Date: 12 June 1979

Signed

A Wayland

Date

9 March 2010

PREM Records Team



CH/EX. REF. NO. B(79)44
 COPY NO. 1 OF 4 COPIES

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

T P Lankester Esq
 10 Downing Street
 London
 SW1

Prime Minister

You asked whether Scotland's share of the
 RSG cut is fair. 11 June 1979

The Scots get a bigger
 RSG relative to British expenditure
 (68% compared with 61% for England and
 Wales), so arguably their cut should be
 bigger. But in fact the £35m. is just about in
 line with population (5.2m. for Scotland against 49.1m.
 for England and Wales).

Dear Tim,

RATE SUPPORT GRANT 1979-80

The Prime Minister asked how the £35 million for the reduction in the RSG cash
 limit for Scotland had been calculated. *Mr. Young is content.*

2. You will remember that the proposal put to Cabinet was that the RSG cash limit
 for England and Wales should be reduced by £200 million. We originally thought in
 terms of reducing the Scottish cash limit by the same proportion as £200 million
 bears to the cash limit for England and Wales. This gave a figure of £30 million.
 The Scots argued for calculating the reduction on the 90:10 ratio which is used for
 dealing with the England and Wales:Scotland shares of comparable FESC programmes
 which would have given a cut of £22 million for the Scots. As a compromise, which
 the Scots accepted, the figure of £25 million was put to Cabinet.

3. In fact Cabinet agreed that the cut for England and Wales should be £300 million
 which would have given a figure, proportionately, of £37½ million for Scotland.
 With the agreement of the Scots, this was rounded down to £35 million because,
 given that the underlying calculation was a bit by and large, £37½ million
looked too precise and would have been difficult to justify publicly. In fact,
 as you will see, £35 million comes out very close to the 90:10 ratio mentioned
 above.

Yours ever,
 M.H.

(M A HALL)

11 JUN 1979



SECRET

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FILE

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10 DOWNING STREET

From the Private Secretary

11 June 1979

P.R.T.

The Prime Minister has considered the Chancellor of the Exchequer's minute of 7 June about the possibility of bringing forward some of the P.R.T. payments which are due in 1980/81 into 1979/80. She is content for this idea not to be included in this year's Budget, but has noted that the Chancellor may wish to consider it for 1980/81.

T. P. LANKESTER

A. M. W. Battishill, Esq.,
H.M. Treasury.

SECRET

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~~Print~~ Print Notice /

This is the detailed breakdown of the expenditure notes.

Treasury Chambers, Parliament Street, SW1P 3AG

Tim Lankester Esq
10 Downing Street
London SW1

11th June 1979

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11/6

Dear Tim,

EXPENDITURE MEASURES PRESS NOTICE

.... I attach an advance copy of the Press Release giving details of the Expenditure measures agreed for 1979/80.

The Press Notice is of course embargoed until after the Chancellor finishes the Budget Speech tomorrow.

I am copying this letter with attachment to the Private Secretaries of other members of the Cabinet.

Yours sincerely,
A C PIRIE

A C PIRIE

and

BUDGET - SECRET

12 June 1979

EXPENDITURE MEASURES IN THE BUDGET

The following is a list of the specific reductions in 1979-80 referred to in the Budget statement :

<u>Department</u> (and principal public expenditure programmes affected)	<u>Description</u>	<u>£ million</u> (at 1979 survey prices)	
Foreign & Commonwealth Office (Programme 2)	Reduction in overseas aid		50
Department of Industry (Programmes 4 and 5)	(i) Four month deferment of payment of approved claims for Regional Development Grant	145	
	(ii) Reduced provision for new commitments by the department and the National Enterprise Board	55	
	(iii) Miscellaneous savings by :		
	Post Office	5	
	British Aerospace	5	
		210	
Department of Energy (Programmes 4 & 5)	(i) Reduction in the non-nuclear research and development budget	2	
	(ii) Reduction in the external financing requirement of		
	BINOC	45	
	British Gas	171	
	National Coal Board	23	
	Electricity Supply Industry (England & Wales)	82	
		323	
Department of Trade (Programme 4)	(i) Abolition of Price Commission, savings on local price surveys, the National Film Finance Corporation, export promotion and tourism	5	
	(ii) The Cooperative Bank agreement to refinance fixed rate export credits currently financed by ECGD	25	
		30	

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<u>Department</u> (and principal public expenditure programmes affected)	<u>Description</u>	<u>Cut £ million</u> (at 1979 survey prices)	
Department of Employment (Programme 4)	Reducing the Manpower Services Commission's programmes and restricting special employment measures		172
Department of Transport (Programmes 5 & 6)	(i) Reduction in British Rail's external financing requirement	14	
	(ii) Reduction in grants for rail freight facilities	1	
	(iii) Roads construction, maintenance, New Towns roads and amenity works	10	25
Department of the Environment (Programmes 7, 8 & 14)	(i) Reduction in public sector housing (England)	300	
	(ii) Savings on community land expenditure	50	
	(iii) Reduction in urban programme	7	
	(iv) Capital expenditure of water industry	55	
	(v) Property Services Agency - reduced expenditure on major new works and purchases	10	
	- reduction in minor works and purchases of furniture and equipment	10	
	- savings in maintenance and running costs	5	437
Department of Education and Science (Programme 10)	(i) Reduction in science budget	5	
	(ii) Abandonment of pilot scheme for grants to 16-18 year olds		10
	(iii) Increase in overseas students' fees	6	
	(iv) Reduction in capital spending	14	
	(v) Reduction in recurrent grant to Universities and Colleges	9	
	(vi) Miscellaneous savings on education	11½	55½

BUDGET - SECRET

<u>Department (and principal public expenditure programme affected)</u>	<u>Description</u>	<u>Cut £ million</u> (at 1979 survey prices)
Office of Arts and Libraries (Programme 10)	Miscellaneous savings	3
HM Treasury (Programme 13)	Reduced provision for expenditure from the National Land Fund	1½
Department of Health & Social Security (Programme 11)	Increase in prescription charges to 45p and certain increased dental charges (Great Britain)	34
Scottish Office (Various Programmes)	Where the Secretary of State has separate responsibilities within his own area for some of the above programmes comparable reductions to be made	76
Welsh Office (Various Programmes)	Where the Secretary of State has separate responsibilities within his own area for some of the above programmes comparable reductions to be made	16
Northern Ireland Office and Department (Programme 15)	Where the Secretary of State has separate responsibilities within his own area for some of the above programmes comparable reductions to be made	35
	Total reduction in programmes	<u>1468</u>

In addition, the contingency reserve is to be cut by £250 million.

PRESS OFFICE

H M TREASURY

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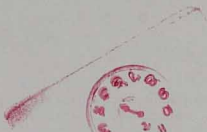
BUDGET - SECRET

NOTES FOR EDITORS

1. In addition to the specific cuts listed in this press notice the budget statement referred to an estimated reduction of £1000m in planned programmes as a result of the cash limits policy announced by the Chancellor of the Exchequer and Minister of State, Civil Service Department, on May 22 and to estimated receipts of £1000 million from disposals of assets during 1979-80.
2. The last complete statement of expenditure plans was published in Cmnd 7439. These cuts are made from the plans as they stood when the Government took Office.
3. 1979 survey prices are in general the prices of autumn 1978 for goods and services. For the external financial requirements of nationalised industries they are average 1978-79 prices. For other transfer payments they are generally an estimated average of 1979-80 prices.
4. Questions on individual items should be addressed to the department concerned.

BUDGET - SECRET

BUDGET & PROFIT



1951

BUDGET & PROFIT

PART 2 begins:-

CST's to π 11.6.79

PART 1 ends:-

Try to π 11.6.79

