



CH/EX. REF. NO. B(79)24 ¹⁵

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

PRIME MINISTER

Accept Chancellor's judgement.
pm

VAT ON PETROL

Prime Minister
The arguments seem to me finely balanced. Are you content to accept the Chancellor's judgement?

At our discussion on 24th May you asked me to examine ways of increasing the revenue paid on the purchase of petrol for business use, by for example replacing the VAT element with a higher rate of specific duty. I find there are great difficulties in achieving what you want in this way but that effectively the same result can be secured by introducing a "blocking" provision to prevent the deduction of VAT on petrol for business use. Any such provision could not, in this context, extend to VAT on diesel road fuel (derv) because of its importance for industrial costs.

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2. It would be technically possible to introduce a "blocking" provision as a Budget measure, to take effect (by Order) on Monday 18th June together with the VAT increase to 15 per cent. It would have to cover all petrol used by businesses: there could be no halfway house - for example, we could not block VAT deduction only in respect of the Budget increase from 12½ per cent to 15 per cent. There might be some difficulties with the EEC, but these could probably be surmounted. The effect of the measure would be to raise additional revenue of about £250 million in a full year and £125 million in 1979/80. The RPI would increase by about 0.2 per cent over time and total UK petrol consumption might be reduced by up to 2 per cent a year in the long run.

4. However, there would be a number of disadvantages:-



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- (i) The revenue gain from the proposal would be reflected in an addition to business costs. This would not be limited to expenditure on petrol for cars, but would extend to other business expenditure on petrol - for example, delivery vans and taxis (which amount to about one-third of all "business use" of petrol). The effect would be very selective and would no doubt give rise to many not unreasonable complaints. We shall be adding to business costs through the 7p excise duty increases for petrol and derv and through the extra VAT on new cars (the subject of an existing blocking Order). I do not think it would be right to do more at this stage - necessarily in a very random fashion.
- (ii) By altering the balance of taxation between petrol and derv, the measure could have a potentially serious effect on the UK car market. As you know, the outlook for our car manufacturing industry is already poor, and we ought not to risk further damage by straining the traditional loyalty of the company car market to British manufacturers. At present, virtually no diesel cars are manufactured in the UK, but output has been increasing elsewhere, especially in France and Germany.



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I am satisfied that a selective (petrol only) increase of this kind could induce a significant switch to diesel cars, with a consequent increase in the volume of imports.

- (iii) Criticism could also be levelled at us on the grounds that the move was much too much of a leap in the dark. We often spoke out in Opposition against ill-considered proposals brought forward in a hurry. I would not like us to be tarred with the same brush. (The blocking Order on cars, to which I have referred above, was part of the original structure of VAT which was the subject of widespread consultation over a long period.)

5. These disadvantages seem to me considerably to outweigh the revenue and energy conservation attractions of the proposal. I have therefore decided not to include the proposal in my forthcoming Budget. Nevertheless, we must clearly expect the energy supply situation to remain tight for some time to come, and there could well be a case in the longer term for a blocking Order (quite possibly applying to Derv as well as to petrol). I propose therefore to instruct officials to give it detailed consideration after the Budget, for possible action either next year or, if the energy supply situation should seriously deteriorate, later this year

G.H.

BUDGET-

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10 DOWNING STREET

From the Private Secretary

4 June 1979

The Prime Minister was grateful for the Chancellor's minute of 1 June in which he set out his main Budget proposals. This is to confirm that she is content with them.

The Prime Minister has also considered the Chancellor's minute of 1 June concerning VAT on petrol. She is content to accept the Chancellor's judgement on this matter, though she has noted that he intends to instruct officials to give it more detailed consideration after the Budget for possible action either next year or, if the energy supply situation should seriously deteriorate, later this year.

The Prime Minister was also grateful for the Chancellor's note, and the accompanying papers by officials, on the forecast.

T. P. LANKESTER

Tony Battishill, Esq.,
HM Treasury.

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