WAYS AND MEANS

Budget Statement

3.45 pm

Mr. Neil Kinnock (Islwyn) (by private notice) : To ask the Chancellor of the Exchequer, whether he will make a financial statement.

The Chancellor of the Exchequer (Mr. Nigel Lawson) : I am happy to respond to the right hon. Gentleman's question.

INTRODUCTION

The background to this year's Budget is the unprecedented strength of the British economy, coupled with the continuing and overriding need to combat inflation, at a time when, throughout the world, it is unmistakably edging up again.

I shall begin with an account of the performance of the economy in 1988 and the prospects for 1989, set in the context of the past 10 years. I shall then deal with monetary policy and the public sector finances. Finally, I shall propose a number of measures to carry forward the process of tax reform.

As usual, the Financial Statement and Budget Report, together with a number of press releases filling out the details of my proposals, will be available from the Vote Office as soon as I have sat down.

ECONOMIC PERFORMANCE AND PROSPECTS

The Government's first 10 years in office have seen a transformation both in the way in which economic policy is conducted, and in the results that have been achieved.

For the first time, economic policy has been set firmly and explicitly in a medium-term context. We have been guided by the basic philosophy that the Government should set a sound medium-term financial framework and leave the private sector free to operate with confidence within it.

The Government came to office with two central objectives--to defeat inflation, and to breathe new life into a moribund economy--and a clear idea of how to achieve those objectives. Inflation is a disease of money ; and monetary policy is the cure. The role of fiscal policy is to bring the public accounts into balance and to keep them there, and thus underpin the process of re-establishing sound money. Strong sustainable growth is achieved, not through any artificial stimulus, but by allowing markets to work again and restoring the enterprise culture ; by removing unnecessary restrictions and controls and rolling back the frontiers of the State ; by reforming trade union law and promoting all forms of capital ownership ; and by reforming and reducing taxation.

The first and most urgent task we faced was to damp down the inflationary fires that had raged in the 1970s, and wrought so much economic and social havoc ; and we succeeded. Between 1974 and 1979, inflation had averaged more than 15 per cent. Over the past six years it has averaged 5 per cent.- -still not good enough, but a massive improvement.

Once business and industry recognised the fundamental changes that were taking place, they responded to the new economic climate with vigour and confidence. As a result, we have experienced the longest period of strong and

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steady growth since the war. Output in the United Kingdom has grown faster than in all the other main European nations during the 1980s--a marked contrast to the previous two decades, when we were bottom of the league--and this growth has been based on a dramatic and sustained improvement in productivity.

For the economy as a whole, our productivity growth has been second only to that of Japan among all the major nations during the 1980s, and our productivity growth in manufacturing has exceeded even that of Japan.

In Britain today we have more people in work than ever before in our history ; they are better motivated than ever before, and their living standards have improved beyond recognition. But it is not just our economic performance that has been transformed : so have our prospects for the future.

Over the past seven years, investment has grown more than twice as fast as consumption, creating the increased capacity necessary to meet future demand. Total business investment is now a higher proportion of national income than ever before, and its quality has improved immeasurably, too ; as has the quality of British management. We have seen a dramatic and long overdue improvement in company profits and a remarkable growth in the total number of businesses, last year at the rate of more than 1,000 a week. Provided we stand firm in our resolve to get on top of inflation, the prospects before us are excellent. At least on this side of the House, we do stand firm.

A year ago, in the aftermath of the worldwide stock market crash, it looked as if there would be some slowing down from the rapid growth of 1987. In fact that was not to be.

As the House knows, the state of the national income statistics leaves much to be desired, but it now appears that we had in 1988 a second successive year of growth at 4.5 per cent., with unemployment falling by over half a million, to well below the European average. Manufacturing output grew particularly rapidly, by more than 7 per cent., to a level well above the previous peak.

But total spending also grew by getting on for 7 per cent., mainly because of the boom in industrial investment, in itself a welcome event, but also because of continued strong growth in consumer spending. This last was financed to an unprecedented degree by borrowing, overwhelmingly mortgage borrowing.

Invevitably, the rapid growth of total spending led to renewed inflationary pressure. To some extent this was diverted into a sharp rise in imports, and hence into the deficit on the current account of the balance of payments. The published figures put this at £14.5 billion in 1988, although, given the £15 billion positive balancing item--another name for errors and omissions--the true figure is almost certainly less than this. But whatever the true figure, it is undoubtedly large, and a sharp increase on the deficit recorded in 1987 after seven successive years of surplus. Given sound policies, however, it can readily be financed.

Moreover, unlike previous current account deficits we have known in this country, it reflects not excessive Government borrowing, but rather an upsurge of private investment unmatched by private savings, and this imbalance is something that will in due course correct itself.

The real threat is posed by the increase in inflation itself. Excluding the distorting effect of mortgage interest

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payments, the RPI rose by 4.5 per cent. last year, much the same as the average over the previous five years, but this underlying rate increased significantly through the year, and now stands at 5.5 per cent.

Moreover, the increase in inflation appears to be a worldwide trend. Taking the seven major industrial nations as a whole, inflation is now at its highest level for three and a half years. In the United Kingdom, as in a number of other countries, it became clear that it was necessary to tighten monetary policy sharply. That meant raising short-term interest rates, which I duly did, starting last June.

I am, of course, keenly conscious of the difficulties many borrowers, particularly home owners, are now experiencing. But however unwelcome high interest rates may be, they are infinitely preferable to the damage that would be done by high inflation. There are now increasing signs that the determined action that I have taken is having the desired effect. The housing boom that played such a large part in the events of last year has subsided. Monetary growth has slowed down appreciably, and retail sales, too, seem to have levelled off over the past four months, presaging a gradual recovery in the personal savings ratio.

The outlook for 1989 is for inflation to rise a little further over the next few months, from 7.5 per cent. including mortgage interest payments, to about 8 per cent., before falling back in the second half of the year to 5.5 per cent. in the fourth quarter and perhaps 4.5 per cent. in the second quarter of 1990.

Some slowdown in real growth is inevitable as we get inflation back on to a downward path--indeed, it has almost certainly already begun to happen. Overall growth is forecast to fall from the 4.5 per cent. recorded last year to 2.5 per cent. this year, with growth through the year at 2 per cent.

Domestic demand is forecast to slow down even more markedly. But within this, investment, which is holding up well, is once again forecast to grow faster than consumption. The current account deficit is forecast to remain at the same level as last year.

But the question of just how "soft" or "hard" the so-called landing will be is not in the hands of Government alone. The Government's task is to reduce inflation by acting, through monetary policy, to bring down the growth of national income in money terms. The task of business and industry is to control their pay and other costs. The more successfully they do so, the less costly in terms of output and employment the necessary adjustment will be.

Over the medium term, however, it is clear from our experience over the past 10 years that the policy we are pursuing will bring inflation down, and steady growth will resume. The best contribution the Government can make to this is to carry forward the process of supply side reform, to help make the economy work better. That is the objective of the specific measures to which I shall turn in the second part of my statement.

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MONETARY POLICY

As I said at the outset, monetary policy plays, and must always play, the central role in the battle against inflation. It is at the very heart of the medium-term financial strategy, the 10th edition of which I am publishing today.

I have described the monetary tightening that has taken place over the past nine months. This has already led to a sharp fall in the rate of growth of the target aggregate, narrow money, or M0. For 1989-90, the target range for M0 will be 1 to 5 per cent., as envisaged in last year's MTFS. Although it will start the year above the top of that range, its very low growth over the past six months--below 3 per cent. at an annualised rate--suggests that it will fairly soon come back within the range. As in the past two years, there is no target for the growth of broad money, or liquidity, but I will continue to take it into account in assessing monetary conditions.

The exchange rate is of particular importance in the conduct of monetary policy. The Government's clear commitment not to accommodate increases in domestic costs by exchange rate depreciation remains a key safeguard against inflation. In this context, we will continue to work with our G7 partners to maintain the greater exchange rate stability that has been a feature of the past two years.

Short-term interest rates remain the essential instrument of monetary policy. I repeat now what I have stated clearly on a number of previous occasions : interest rates will stay as high as is needed for as long as is needed, for there will be no letting up in our determination to get on top of inflation.

PUBLIC SECTOR FINANCES I now turn to fiscal policy. When we first took office, the public sector borrowing requirement was over 5 per cent. of GDP--equivalent to £25 billion in today's terms. This we steadily reduced over the years as a deliberate act of policy, until, by 1987-88, the PSBR had been eliminated altogether, and we started to repay the public debt.

Accordingly, last year I budgeted for a further public sector debt repayment, or PSDR, of some £3 billion. In the event, it looks like turning out between four and five times as large, at £14 billion, or 3 per cent. of GDP.

Even if there had been no privatisation proceeds at all, the public finances would still be in surplus, to the tune of some £7 billion. Nothing like this has ever been achieved in the past 40 years. Indeed, Government debt as a proportion of GDP is now lower than at any time since the first world war, and no other major country enjoys a comparable budget surplus. It has not been easy, even though we have been assisted this year by the exceptional buoyancy of the economy, which both boosted tax receipts and reduced public expenditure. Moreover, the substantial net repayment of public debt over the past two years has permanently reduced the burden of debt servicing, both now and for future generations. For the coming year, for example, the debt repayments of the last two years mean that net debt interest costs will be lower by over £1.5 billion a year. This saving is being put to good use, allowing extra spending on departmental programmes within our overall public expenditure constraints.

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The dramatic improvement in the United Kingdom's public finances has also provided a welcome opportunity to devote more attention to the structure of the debt that remains. We will continue to seek both to minimise the cost of servicing the Government's domestic debt and to improve its quality by relying less on the more liquid borrowing instruments.

We have also been able to restructure part of the Government's foreign currency debt, launching an innovative and cost-effective programme of Treasury bills denominated and payable in ECU. The first series of six- monthly tenders for these bills has proved a highly successful innovation. We plan to continue the programme at around the current level.

Meanwhile, I am today adding one more entry to the long list of financial controls which we have swept away during our term of office. The last surviving relic of the post-war apparatus for the direction of capital by the state is the Control of Borrowing Order, which, since 1946, has involved, first, the Treasury and, then, the Bank of England in giving consents for equity and bond issues in the capital markets.

As from today, it will no longer be necessary for companies wishing to make capital market issues to obtain the Bank of England's consent to the timing of such issues. The new issue queue will be a thing of the past. As soon as practicable, we will revoke the order itself and repeal the 1946 Act from which it stems.

The sterling capital market has in recent times been going through a period of considerable adjustment, as the Government have changed from being a large issuer to a large purchaser of their own debt. The abolition of the Control of Borrowing Order will remove an unnecessary and bureaucratic restriction on issuers of capital as they move into the space formerly occupied by the Government when they were a borrower.

This new freedom will be enhanced by a further, important set of deregulatory measures for the sterling capital market which are being promulgated today in notices issued by the Bank of England. These measures will open up the market for sterling paper of less than five years' maturity by extending the range of institutions which can make such issues ; and they will create a unified regime for all these issues.

Taken together, the changes I have described constitute a major liberalisation of the arrangements for London's capital markets. They will give greater flexibility to issuers and wider choice to investors.

In last year's Budget speech, I set out the principle of a balanced budget as the proper objective of fiscal policy, in these terms : "A balanced Budget is a valuable discipline for the medium term. It represents security for the present and an investment for the future. Having achieved it, I intend to stick to it. In other words, henceforth a zero PSBR will be the norm. This provides a clear and simple rule, with a good historical pedigree".--*[Official Report, 15 March 1988 ; Vol. 129, c. 996.]*

It is a rule that ensures that, as national income continues to rise, the ratio of public debt to national income continues to fall, and with it the burden of debt interest. It ensures, too, that the state makes no claim either on the savings of the private sector or on flows of finance from overseas.

To go further than this, and seek to achieve the maximum possible repayment of public debt, would not be consistent with the Government's policy, as it would mean

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deferring for a very long time the benefits of a reduction in the burden of taxation, so I reaffirm the principle of the balanced Budget. However, given the substantial surplus we now have, the path of prudence and caution must be to return to balance not overnight, but gradually, over a period of years. Thus, we can expect further years of debt repayment ahead of us.

Moreover, given the particular uncertainties there are at the present time, I believe it would be right to budget for 1989-90 for a surplus similar to that secured in the year now ending ; in other words, a further public sector debt repayment, or PSDR, of some £14 billion.

This means that, in the space of three years, we shall have repaid roughly a sixth of the public debt that has accumulated over more than two centuries, but it also means that it will not be possible in this year's Budget to reduce the burden of taxation ; that is to say, to reduce taxation as a share of national income.

TAXPAYER CONFIDENTIALITY

Before I turn to my proposals for changes in taxation, I have one other change of a specific nature to announce.

As the House knows, the new official secrets legislation currently passing through Parliament is very much narrower in scope than the present Official Secrets Act. In particular, it does not cover information in the possession of either the Inland Revenue or Customs and Excise concerning the private affairs of specific taxpayers. I am sure that the whole House will agree that it is essential for taxpayer confidentiality to be properly protected.

I therefore propose to introduce provisions in this year's Finance Bill to ensure that it will continue to be a criminal offence for officials or former officials of either of the Revenue Departments to reveal information about the private affairs of a specific taxpayer. I would only add that the need for this protection is in no sense a reflection on the probity and integrity of the members of those two Departments.

Indeed, after nearly six years as Chancellor and more than eight years as a Treasury Minister, I would like to take this opportuntiy to pay public tribute to the outstanding service I have consistently received from the officials of both Departments.

Mr. Eric S. Heffer (Liverpool, Walton) : Will the right hon. Gentleman give way?

BUSINESS TAXATION

Mr. Lawson : I now turn to taxation. As I have done on a number of previous occasions, I propose to divide this into three broad sections : the taxation of business, the taxation of savings, and the taxation of personal income and spending.

First, taxes on business. Ever since the corporation tax reform I introduced in 1984, the rate of corporation tax for small companies, defined for this purpose as those with annual profits of less than £100,000, has been set at the basic rate of income tax, currently 25 per cent.

Large companies, defined as those with profits of £500,000 or more, pay the main rate of corporation tax of 35 per cent., one of the lowest rates of tax on company profits in the world. Between £100,000 and £500,000, the averge rate of tax gradually rises from 25 to 35 per cent.

I propose to keep the small companies rate in line with the basic rate of income tax for 1989-90 and to leave the main corporation tax rate unchanged, but I propose to increase the small companies' rate band substantially, by 50 per cent.

Thus, the small companies' rate will apply to companies with profits of less than £150,000, and the 35 per cent. rate will be reached only at profits of £750,000. These changes will reduce the corporation tax burden for more than half of all those companies that do not already enjoy the benefit of the small companies rate. I propose to increase the VAT threshold to £23,600, the maximum permitted under European Community law.

I also have to set the scales for the private use of company cars. This remains far and away the most widespread benefit in kind. When I doubled the car scales in last year's Budget, I made it clear that this still left this benefit significantly undertaxed. Accordingly, I propose to increase the car scales by one third for 1989-90. The yield from this will be £160 million in 1989-90 and £200 million in 1990-91. There will be no change in the fuel scales.

Over the years, I have received a number of representations from business complaining about the long-standing tax treatment of foreign exchange gains and losses. I recognise that, as business becomes more global, this subject becomes increasingly important. However, I have to say that I find it one of the most intractable I have encountered. Certainly, there can be no question of any change in the present system until a number of crucial and complex issues have been satisfactorily resolved. I have therefore authorised the Inland Revenue to publish today a consultative document which explores those issues and examines the scope for reform.

Finally, on business taxation, I have two major simplifications to propose, both of which follow from the income tax reforms that I introduced in last year's Budget.

One of the many undesirable features of an income tax system with several higher rates was that, since a taxpayer's marginal rate could well be very different in different years, the question of which year income related to made a great deal of difference. This was true of schedule E, where the strict rule is that income is taxed in the year to which it relates, on an accruals basis.

For the vast majority of employees, this basis of assessment for schedule E poses no problem, but for about half a million people, mainly directors, who do not receive all their income in the year to which it relates, it causes complications and often needless assessments and correspondence long after the tax year is over. It is also open to manipulation.

I therefore propose that income tax under schedule E should in future be assessed on a receipts basis, with the simple principle that one pays the tax when one receives the income. This will have a transitional cost of £80 million in 1989-90 and £60 million in 1990-91, but in the long term it will yield both extra revenue and a significant saving in both taxpayers' time and Inland Revenue staff. The reduction in the top rate of income tax to 40 per cent. in last year's Budget also enables me to make a major simplification of the tax regime for the vast bulk of the incorporated sector of small businesses : those known as close companies-- generally speaking, unquoted companies that are controlled by five or fewer people.

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The rules for the so-called apportionment of close companies' income are notoriously complex, taking up some twenty pages of impenetrable legislation. These rules are no longer needed, and I propose to abolish them. I believe that family businesses in particular will welcome this substantial simplification.

I do, however, have to guard against the avoidance of tax on investment income by channelling it through a closely controlled investment company. Any such company which does not distribute the bulk of its profits and other investment income will therefore be taxed at 40 per cent., equivalent to the higher rate of income tax.

TAXES ON SAVING

I now turn to the taxation of saving.

The sharp decline in the ratio of personal saving to personal income, over the past two years in particular, has led to even more discussion than usual of the merits of providing greater tax incentives for personal saving.

Certainly it is desirable that, over the medium term, we generate as a nation a level of saving sufficient to finance a high level of investment, but what matters for that is not personal saving alone, but corporate saving too, which is running at a historically high level, and public sector saving, which has been boosted by the move to budget surplus.

Moreover, the personal saving ratio is measured in terms of gross saving net of borrowing, and it has fallen not because of a decline in gross saving but as a result of the sharp increase in personal borrowing. The appropriate remedy for that is to raise the cost of borrowing, and with it the return on savings, as we have done. Above all, the role of tax reform is to encourage enterprise and improve economic performance in the medium term. It is wholly inappropriate as a response to short-term or cyclical phenomena. So for the taxation of savings, the Government's policy is clear : it is to strengthen and deepen popular capitalism in Britain, by encouraging, in particular, wider share ownership. I have a number of specific tax measures to announce today to that end.

Personal equity plans, or PEPs, were first announced in my 1986 Budget, and started up in January 1987. As the House knows, those who invest in these plans pay no further tax at all, either on the dividends they receive or on any capital gains they may make--indeed, there is no need for them to get involved with the Inland Revenue at all.

Personal equity plans got off to a good start, with over a quarter of a million investors, many of whom had never owned shares before, subscribing almost £500 million between them in 1987.

Since then, however, the take-up of new PEPs has slowed down, not least as a result of the changed climate in the equity market which followed the October 1987 stock exchange crash. So the time has come to improve and simplify PEPs and give them a new boost.

First, I propose to raise the annual limit on the overall amount that can be invested in a PEP from £3,000 to £4,800. Secondly, within that, I propose to raise substantially the amount that can be invested in unit trusts or investment trusts. For many small savers, these provide an excellent introduction to shareholding.

At present, PEP investors are limited to £540 a year, or a quarter of their PEP, whichever is the greater, in unit or investment trusts. I propose to increase this limit very

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substantially, to £2,400 a year ; and the whole of a PEP will be able to be invested in unit or investment trusts, up to this limit. To qualify for tax relief, the unit or investment trusts will be required to invest wholly or mainly in United Kingdom equities. Thirdly, at present, only cash may be paid into a PEP. I propose that investors should also be permitted to place directly into a PEP shares obtained by subscribing to new equity issues, including privatisation issues.

Finally, I propose to make a number of important simplifications to the PEP rules so as to make the scheme more flexible, better directed to the needs of small and new investors, and, above all, cheaper to administer.

I am confident that the changes that I have announced today will enable personal equity plans to play an important part in stimulating the spread of ownership of British equities in the years ahead. I also have a number of improvements to announce specifically designed to encourage employee share ownership.

It is a striking fact that the number of approved all-employee share schemes has risen from a mere 30 in 1979 to almost 1,600 today, benefiting some 1.75 million employees. At present, the annual limits on the value of shares which can be given under all-employee profit-sharing schemes are £1,250 or 10 per cent. of salary up to a ceiling of £5,000. I propose to raise these cash limits to £2,000 and £6,000 respectively.

Secondly, I propose to increase the monthly limit on contributions to all- employee save-as-you-earn share option schemes from £100 to £150, and at the same time double the maximum discount from market value at which options may be granted from 10 per cent. to 20 per cent.

Thirdly, a number of my hon. Friends have been concerned that current tax law may be inhibiting the development of employee share ownership plans, otherwise known as ESOPs. These are distinguished from ordinary approved employee share schemes by the fact that they use a wider variety of finance, acquire more shares and tend to operate on a longer time scale.

I propose to make it clear that companies' contributions to ESOPs qualify for corporation tax relief, provided only that they meet certain requirements designed to ensure that the employees acquire direct ownership of the shares within a reasonable time. I hope that this will encourage more British companies, particularly in the unquoted sector, to consider setting up ESOPs.

Those firms with employee share ownership schemes have no doubt that giving the work force a direct personal interest in their profitability and success improves the company's performance. The same benefits flow from profit-related pay. That was one of the reasons why, in my 1987 Budget, I introduced a tax relief to encourage its development. I have some improvements to make to this scheme, too.

First, as I have previously announced, I propose to abolish the restriction that, to qualify for the tax relief, prospective profit-related pay must equal at least 5 per cent. of total pay. Secondly, I propose to raise the limit on the annual amount of profit-related pay which can attract relief from £3,000 to £4,000. Thirdly, I propose to enable employers to set up schemes for headquarters and other central units using the profits of the whole company or group for their profit calculations. Fourthly, to help share schemes and ESOPs

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as well as profit-related pay, I propose to change the so-called material interest rules which may at present unnecessarily exclude employees from schemes where they can already benefit from a trust set up for employees.

Taken together, the package of measures I have announced to encourage wider share ownership in general, and employee share ownership in particular, will help to ensure that the idea of a share-owning democracy becomes ever more entrenched as a part of the British way of life.

I now turn to life assurance. Last June, the Inland Revenue issued with my authority a major consultative document on the taxation of life assurance. The tax regime for life assurance is unique. The present system dates back to the first world war and has developed over the years in a piecemeal way, leading to a state of affairs in which the incidence of tax is extremely uneven, with some life offices paying no tax at all.

There is clearly a powerful case for reform, with a view to securing a tax regime which is more equitable both within the industry and as between life assurance and most other forms of savings.

I have considered very carefully the representations that the industry has made, and taken full account both of the changes to the regulation of life assurance proposed by the Securities and Investment Board under the Financial Services Act 1986 and the prospects for increased competition within the European Community after 1992. In the light of these factors, I have decided not to proceed with the more radical reforms canvassed in the consultative document, but I do have number of important changes to propose, based for the most part on the general tax reform principle of seeking lower rates on a broader base.

First, many life offices write pension business as well as life assurance, and they are not required to keep the two businesses entirely separate for tax purposes. This enables them to set the unrelieved expenses of the pensions business against the income and gains of their life business, thus giving their life profits unduly favourable tax treatment. The life offices themselves have accepted that this treatment is anomalous, and I propose to end it. This change will come into force on 1 January 1990. Together with some related measures to put the taxation of life offices' pension business on to a proper footing, it will yield some £150 million in 1990-91.

The remainder of the changes that I have to propose constitute a broadly balanced package which, because of the transitional provisions, will reduce the taxation of life assurance in 1990-91 by some £100 million.

I propose that the expenses incurred by life offices in attracting new business should continue to be fully deductable for tax purposes from the income and gains of life funds, but should in future be spread over a period of seven years. To give the industry time to adjust, this change will be phased in gradually over the next four years, starting on 1 January, 1990.

There are certain other, more technical, matters raised in the consultative document which will require further discussion with the industry, and any legislative changes on these issues will have to wait for next year's Finance Bill. But I can say here and now that I propose, as from 1 January 1990, to abolish life assurance policy duty. I also propose, from the same date, that the rate of tax payable on the policyholders' share of the income and gains of life offices, which at present stands at 35 per cent. on

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unfranked investment income and 30 per cent. on realised capital gains, should be reduced to the basic rate of income tax. The net effect of all these changes to the taxation of life assurance will be a cost of £20 million in 1989-90 and a yield of £45 million in 1990-91, rising somewhat in subsequent years. But above all, it will provide a more efficient and equitable tax regime for this most important industry.

Later this year, United Kingdom unit trusts will be able to compete freely in Europe and will face competition from analogous Community investment schemes here. At present, trusts investing in gilt-edged securities or other bonds face a tax disadvantage. They pay corporation tax at 35 per cent. on their income but can pass on a credit of only the basic rate of income tax to their investors. I therefore propose that from 1 January 1990, as for life assurance companies, the corporation tax rate on unit trusts that come within the new European Community rules will be equal to the basic rate of income tax. Their investors will then get full credit for all the United Kingdom tax the trusts pay.

I turn now to pensions. The tax treatment accorded to occupational pension schemes is particularly favourable ; and the extent of this privilege has to be circumscribed by Inland Revenue rules. Thus, pension, schemes qualify for tax relief only if they meet certain conditions, notably that the pension paid may not exceed two thirds of final salary : and if they fall foul of any of these rules, they lose all relief.

This has the perverse result that tax law effectively constrains the overall pension an employer can pay his employee. This is neither desirable nor necessary. Accordingly, I propose to make it possible for employers to provide whatever pensions package they believe necessary to recruit and reward their employees.

However, while it is clearly right that employers should be free to provide whatever pension they see fit, it would not be right to make the present generous tax treatment open-ended. I therefore propose to set a limit on the pensions which may be paid from tax-approved occupational schemes, based on a final salary of £60,000 a year. I have deliberately set the ceiling at a level which will leave the vast majority of employees unaffected, and it will be subject to annual uprating in line with inflation. It will still be possible for a tax-approved occupational scheme to pay a pension of as much as £40,000 a year, of which up to £90,000 may be commuted for a tax-free lump sum.

The new ceiling will apply only to pension schemes set up on or after today, or to new members joining existing schemes after 1 June. Public sector schemes, too, will be amended to comply with this. As I have already said, there will now be complete freedom to provide benefits above the Inland Revenue limits, though without the tax relief.

The introduction of this ceiling on tax relief also enables me to simplify and improve the rules for the majority of pension scheme members, in partcular to ease the conditions under which people can take early retirement.

I also propose to simplify very substantially the rules concerning additional voluntary contributions to pension schemes, or AVCs. In particular, the present requirements for free-standing AVCs place a heavy administrative burden on employers. These requirements will be greatly reduced. Indeed, in many cases employers will not need to be involved at all.

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Furthermore, if AVC investments perform very well, occupational pensions may at present have to be reduced to keep total benefits within the permitted limits. I propose that, in future, any surplus AVC funds should be returned to employees, subject to a special tax charge. This will remove the penalty that at present exists on good investment performance.

The most important development in pensions in recent years has undoubtedly been the introduction and success of personal pensions. Since July last year, 1 million people have already taken advantage of the new flexibility and opportunities these offer. I have two proposals today to make personal pensions still more attractive. First, I propose to make it easier for people in personal pension schemes to manage their own investments. Second, I propose to increase substantially the annual limits, as a percentage of earnings, on contributions to personal pensions by those over the age of 35. This will be of particular value to those running their own businesses, who are often unable to make contributions until later on in their working life. It will also improve the position of personal pensions in relation to occupational schemes. The new limits will be subject to an overall cash ceiling based on earnings of £60,000, corresponding to the new ceiling for occupational pensions, and similarly indexed.

These changes build on, and complete, the pension measures I introduced in my 1987 Budget. They represent a significant deregulation which will allow more flexibility, while setting for the first time a reasonable cash limit on the tax relief available to any individual. They should give a boost, in particular, to saving through personal pensions and through AVCs.

Coupled with the changes I made in 1987, this is as far as I wish to go in amending the tax treatment of pensions.

Finally, on the taxation of saving, it should not be overlooked that a far- reaching reform which I announced in last year's Budget, to come into effect in April 1990, is relevant in this context. I refer to independent taxation, about which three new explanatory leaflets are now available from all tax offices.

There can be little doubt that one of the greatest disincentives to saving in the present tax system is the treatment of the savings of married women. At present a wife's income from savings has to be disclosed to her husband, and taxed at his marginal rate. Independent taxation will change all that. In particular, those married women who have little or no earnings will in future have their own personal allowance to set against their savings income. Independent taxation may well do much to encourage the growth of personal saving in this country.

TAXES ON SPENDING

I now turn to taxes on personal income and spending. As the House knows, Her Majesty's Government are obliged to implement the European Court's judgment that certain of our zero rates of VAT on supplies to business, notably on non-residential construction, but also on fuel and power and on water, are not lawful. This derives from the court's interpretation of the Community's sixth VAT directive, to which the United Kingdom agreed in 1977. The necessary changes will be introduced in this year's Finance Bill, and draft clauses have already been published.

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In implementing the judgment, I have sought to do as much as possible to minimise the burden. From 1 April, VAT will be payable in respect of all non-residential construction, unless carried out under agreements entered into before the court ruling. As from 1 August, landlords will have the option to tax rents, which means, in practice, that in most cases no extra VAT will be paid at all.

These measures will reduce the burden of VAT on construction, so far as the private sector is concerned, to just £35 million in 1989-90, rising to £110 million in 1992-93. Without them, the yield from VAT on construction in the private sector would have risen to £450 million. There will also be a first-year yield of £250 million from construction carried out for the public sector, and the public sector programmes concerned have already been protected by compensatory adjustments where necessary.

So far as water for industry and fuel and power for business use are concerned, VAT will not be payable until July 1990. VAT on fuel and power will apply to business users above a specified threshold. Private households will remain zero-rated.

I have been particularly concerned about the impact of the European Court's ruling on charities. Unfortunately, charities' business activities cannot lawfully be shielded from the effects of the ruling, but I have been able to retain zero rates for construction, water, fuel and power for all charities' non-business activities, for churches, and for residential accommodation such as hospices, students' hostels and old people's homes.

I have considered whether there is anything further I can sensibly do to assist charities with their VAT bills in these special circumstances. I propose to relieve charities from VAT on fund-raising events, on sterilisng equipment for medical use, and on classified advertising.

I also propose to relieve from car tax cars leased to the disabled. This is equivalent to an overall saving of about £400 on each vehicle leased to a disabled person. However, in general, I continue to believe that the best way of helping charitable causes through the tax system is by directly encouraging the act of charitable giving. The payroll giving scheme, which I introduced in my 1986 Budget, has been growing steadily. Some 3,400 schemes have now been set up, and over 100,000 employees are already participating, quite a few of them giving the full £240 annual limit for tax relief. I now propose to double that limit to £480, or £40 a month.

I now turn to the excise duties. For some years now, the potential damage to the environment in general, and the risk to child health in particular, from excessive lead in the atmosphere has been a matter for concern. Lead in petrol accounts for 80 per cent. of lead in the atmosphere. The Government are firmly committed to phasing out leaded petrol, and in successive Budgets I have sought to assist this. I first introduced a tax differential in favour of unleaded petrol in 1987, and I increased it last year, but, although sales are undoubtedly rising, unleaded petrol still accounts for only some 5 per cent. of total petrol sales, even though two- thirds of the cars now on the road could use it, either without any modification, or else with only a minor modification, which should not usually cost more than £20 and, in many cases, will be carried out free. One of the problems is ignorance of the facts. Many motorists do not realise that their cars can already use unleaded petrol. Othes are unaware of how modest the

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modification cost usually is, and many are under the false impression that if they do switch to unleaded petrol, their cars will no longer be able to use leaded petrol.

It is clearly essential that these myths are rapidly dispelled. Meanwhile, I propose to take the opportunity of this Budget to increase still further the tax differential in favour of unleaded petrol, by nearly 4p a gallon. This means that, at a shade over 14p a gallon, or more than 3p a litre, our tax differential in favour of unleaded petrol will be greater than that of any other country in the European Community, with the solitary exception of Denmark. If the benefit of today's change is fully passed on to the customer--and I look to the oil companies to see that it is--it means that the price of unleaded petrol at the pump will generally be getting on for 10p a gallon, or just over 2p a litre, cheaper than four-star leaded petrol.

But I do not intend to stop there. I also propose to raise the tax on two and three-star petrol, so that the pump price of these grades will be at least as high as that of four-star.

This should encourage garages to phase out two-star petrol, which is already down to about 6 per cent. of the total market, thus enabling them to switch storage capacity, and in some cases pumps too, to unleaded petrol --quite apart from the incentive to the remaining two-star users to switch to unleaded fuel.

I am confident that the duty changes I have announced, which will take effect from six o'clock this evening, will contribute to a marked increase in the use of unleaded petrol over the next 12 months. They will also lead to a loss of revenue of some £40 million in 1989-90. I propose to recoup this from vehicle excise duty. At the present time, a bus or a coach has to have 66 seats before it pays as much in vehicle excise duty as a family car. I propose to rectify this anomaly by increasing the tax rates of this group of vehicles so that they cover their track costs. I also propose to increase the rates of duty for the heaviest non-articulated lorries, to put them on a more equal footing with articulated lorries. At the same time, I propose to simplify the system, greatly reducing the number of separate rates of vehicle excise duty.

I have no further changes to propose this year in the rates of excise duty.

INCOME TAX

Nor do I propose any change this year to either the basic or higher rate of income tax.

Since I aligned the rates of income and capital gains tax in last year's Budget, it follows that I also propose no change this year in the capital gains tax rates. However, I do have a few announcements to make concerning capital gains tax.

With the advent of independent taxation from April 1990, married women will acquire their own capital gains tax threshold, so that a married couple will enjoy two such exemptions. In the light of this, I propose to maintain the capital gains tax threshold at £5,000 for 1989-90.

Secondly, I propose to abolish the general holdover relief for gifts. This was introduced by my predecessor in 1980, when there was still capital transfer tax on lifetime gifts, in order to avoid a form of double taxation, but the tax on lifetime giving has since been abolished, and the relief is increasingly used as a simple form of tax avoidance. However, while the general holdover relief will

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go, I propose to retain it for gifts of business, farm and heritage assets ; and, of course, gifts between husband and wife will continue to be exempt.

Moreover, I propose to extend the existing relief for all gifts to charities and to gifts of land and buildings to housing associations. Where, instead of being given away, the land is sold at less than market value, any capital gains tax will be based on the actual proceeds rather than, as now, on the market value. I also propose that such gifts and concessionary sales be normally exempt from inheritance tax.

In the case of gifts of personal belongings, these benefit from chattels relief, under which any items worth less than £3,000 on disposal are entirely exempt from capital gains tax. I propose to double the chattels exemption limit to £6,000.

Thirdly, I propose to change the tax treatment of certain bonds so as to simplify the tax rules and prevent a loss of yield by the use of indexation to create losses and the conversion of income into capital gains.

To return to income tax, I propose to raise all the main income tax thresholds and allowances by the statutory indexation factor of 6.8 per cent., rounded up. Thus, the single person's allowance will rise by £180 to £2,785, and the married man's allowance will rise by £280 to £4,375. The basic rate limit will rise by £1,400 to £20,700. The single age allowance will rise by £220 to £3,400, and the married age allowance by £350 to £5,385. The higher level of age allowance will rise by £230 to £3,540 for a single person, and by £360 to £5,565 for a married couple.

I have a number of measures to help the elderly. In 1987 I introduced a new and more generous age allowance for those aged 80 and over. I now propose to extend it to include all those aged 75 and over. This will take an additional 15,000 elderly single people and married couples out of tax altogether. Three quarters of all those aged 75 and over will not be liable to income tax at all. The income limit for the age allowance will rise by £800 to £11,400, again in line with indexation. However, I propose to reduce the rate at which age allowance is withdrawn above this income limit. I propose that, in future, it should be withdrawn at the rate of £1 of allowance for each £2 of income above the limit, instead of the present rate of £2 for every £3. This means that the marginal tax rate for those in the withdrawal band will be reduced to well below 40 per cent., thus meeting a large number of representations I have received over the past year.

The Finance Bill will also include the provisions to establish the new tax relief for the over-60s' health insurance premiums, which I announced to the House in January, and which will take effect from April next year, at a cost of £40 million in 1990-91.

I have one further change to make to help pensioners. Under the earnings rule, any pensioner who decides to continue to work after reaching the statutory retirement age sees his or her pension docked at a rate of 50 per cent. on every £1 earned between £75 and £79 a week, rising to 100 per cent. for every £1 earned over £79 a week. This rule applies until he or she has reached five years beyond the state pension age.

The manifesto on which we were first elected in 1979 acknowledged that it was wrong to discourage people who wished to work beyond retirement age in this way, and we pledged that we would abolish the earnings rule. That is precisely what we shall do. My right hon. Friend the

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Secretary of State for Social Security and I have agreed that the pensioners' earnings rule should be abolished from the beginning of October, the earliest practicable date. The necessary legislation will be included in the Social Security Bill currently before the House.

The cost to public expenditure will be £190 million in 1989-90, which will be entirely met from the Reserve, but the net cost of this measure will be significantly reduced by the income tax payable on the increased pensions.

Those who wish to defer taking their pension will remain entirely free to do so, and will continue to earn a higher pension in return. I am sure the whole House will welcome this long-overdue reform. If I were to adopt the so-called "duck test" now in vogue across the Atlantic, the pensioners' earnings rule would probably qualify as a tax, and I would now be able to claim to have abolished a sixth tax, but sound tax principles, coupled with my innate modesty and natural reticence, prevent me from doing so.

NATIONAL INSURANCE CONTRIBUTIONS

I have one further measure to propose. It has long been a feature of the national insurance system that, once people earn more than the lower earnings limit, which in 1989-90 will be £43, they have to pay national insurance contributions at the same rate on the whole of their earnings up to the upper earnings limit. There are currently three different rates--5 per cent. and 7 per cent. for those on lower pay, and the standard rate of 9 per cent. The two reduced rates, which I introduced for both employers and employees in my 1985 Budget, cut the cost of employing the young and unskilled, among whom unemployment was then high and rising, and cut the burden of national insurance contributions on the low paid.

However, the highly desirable reduction in the steep step at the lower earnings limit was achieved at the expense of creating two small steps further up the earnings scale. This is not a real problem so far as employers' contributions are concerned, but it is for employees. For it inevitably means that, at certain points on the income scale, people can still be worse off if they earn more. Their extra earnings take them from a lower rate band to a higher one, and they therefore lose more in national insurance contributions than they gain in extra pay.

In agreement with my right hon. Friend the Secretary of State for Social Security, I now propose to build on my 1985 reform. For pretty well everyone who pays employee national insurance contributions, I propose to reduce to only 2 per cent. the rate of contributions on their earnings up to and including the lower earnings limit. On their earnings above that limit, there will be a single rate of 9 per cent., up to the upper earnings limit, which has already been set for 1989-90 at £325 a week. This will abolish altogether the steps which at present exist at earnings, for 1989-90, of £75 and £115 a week, and thus remove a serious work disincentive from the system. The step, which has always existed at the lower earnings limit, where people first come into the national insurance system, is the entry ticket to the full array of contributory benefits--as such, it is an essential feature of the contributory principle--but my proposals will more than halve this step, to only 86p a week in 1989-90. There will be no change in the contributions payable by employers.

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This reform will significantly reduce the burden of employees' national insurance contributions across the board. For the lowest paid, that burden is now heavier than the burden of income tax. This is the most effective measure I can take to lighten it. For everyone on just under half average earnings and above, it will leave them £3 a week more of their own money.

The new system will take effect from the beginning of October, the earliest practicable date. The cost will be £1 billion in 1989-90 and £2.8 billion in 1990-91. The necessary legislation will be included in the Social Security Bill currently before the House.

The total additional cost of all the measures in this Budget, on an indexed basis, is under £2 billion in 1989-90 and £3.5 billion in 1990- 91.

CONCLUSION

In this Budget I have reaffirmed the Government's commitment to the defeat of inflation through the maintenance of prudent monetary and fiscal policies. I have budgeted for a debt repayment of £14 billion--the largest ever. I have announced a major reform of, and reduction in, employees' national insurance contributions ; and I have honoured our pledge to abolish the earnings rule for pensioners.

I commend this Budget to the House.

Mr. Kinnock : I begin with customary felicitations and, on this occasion, thank the Chancellor of the Exchequer for his reply to my private notice question. I shall try to ensure that my supplementary is not as long as the answer he gave me.

I also take this opportunity to welcome the change that the right hon. Gentleman has announced in the excise duties, a change that will promote the use of lead-free petrol. That is an entirely sensible step for the Chancellor to take. On behalf of my hon. and right hon. Friends, I further welcome the belated achievement, after 10 years in government, of the Conservative pledge to abolish the earnings rule for pensioners. It is only a fortnight since my hon. Friends on the Social Security Bill Committee sought, not for the first time, to secure that abolition. It is a shame that the Government did not see fit, even at that juncture, to make the adjustment so that at least it could have been an act of consensus, which I am sure it will be. This is not simply an annual Budget ; the occasion is becoming marked by what can only be described as the custom of holding the annual nationalist games. I hope that that custom will not last very long because it is of no use to anybody, least of all the people of Scotland and Wales. In any case, we did not have to rely on the nationalists for entertainment when we had a professional juggler right in front of us.

After nearly six years as Chancellor of the Exchequer, the right hon. Gentleman was able to stand up this afternoon and say that inflation in the second half of this year will reach 8 per cent. and that then it is expected to dip. He is so afraid of what will actually happen that he dare not raise any excise duties. He announced that growth in the course of this year will be halved and that the balance of payments deficit will stay the same this year as it was last year--that is, around about £15 billion. He said that he expected interest rates to remain high. But still, after announcing all this wonderful record of his

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achievements, particularly in the past 12 months, the right hon. Gentleman produced again the lexicon of cliche s about an unprecedented strength in the economy.

Yet again, in the next 12 months, we shall see just how much strength the right hon. Gentleman will produce in the economy. A year certainly does make a difference. Last year we had the boom budget that made the credits spree and the trade deficit and inflationary pressures worse than they otherwise would have been. This year we have had the bust Budget--a botched attempt to make up for the Chancellor's excesses and messes in last year's Budget.

Last year, in his Budget forecasts, the Chancellor told us that, in 1988, inflation would be 4 per cent., but he said that that was still too high. It was 6.8 per cent. in 1988 and it is now 7.5 per cent. and he has just told us that it will rise further. Of course, it might dip a little towards the back end of the year, perhaps even as early as July, because of the arithmetic of the year-on-year calculation of inflation. The fact remains, however, that without any excuse of any major move in commodity prices and without the pressure of any major movement in oil prices such as the previous Labour Government had to put up with, this is a Chancellor who is fast becoming Mr. Inflation.

Last year, the Chancellor, as usual, missed his monetary targets--missed them by billions. In his estimate of the Budget surplus at £3 billion, he showed that he had absolutely no idea of what was happening in the economy--he was out by a factor of five. Last year, the Chancellor proved that he is to economic forecasting what Eddie the Eagle is to ski jumping.

There will, as usual, be much comment on the Budget, but I warrant this : this year no one, neither the Chancellor's friends nor the Prime Minister-- there is a distinction--will say that this Budget was "quite the most brilliant we have seen"

After the experience of the past 12 months, perhaps the Prime Minister knows the difference between brilliance and flashiness, but the less lustrous Budget of 1989 cannot be blamed on any lack of advice. There has been no shortage in either the quantity or the quality of that advice.

The Chancellor of the Exchequer has received advice from his right hon. Friends the Members for Henley (Mr. Heseltine), for Shropshire, North (Mr. Biffen), and for Chesham and Amersham (Sir I. Gilmour) and had the benefit of advice from his right hon. Friend the Member for Woking (Mr. Higgins)-- whose advice is of high quality--and he has also had the benefit of advice from his right hon. Friend in the Cabinet, the Secretary of State for Wales, but he ignored that advice as well. He has also had high-quality advice from his right hon. Friend the Member for Old Bexley and Sidcup--the good old Member for Bexley and Sidcup, say we, because he tendered very high-quality advice to the Chancellor. However, the Chancellor has dismissed all his right hon. Friends as if they were a bunch of

"teenage scrbblers". The Chancellor was right about one thing last year ; he was absolutely right to scorn the estimates offered in July by the City analysts that the balance of payments deficit for 1988 would be £10 billion. They were totally wrong about that ; it was £14.7 billion, so the Chancellor was right to scorn them. Let us hope that he does not berate them quite so frequently this year because though they were far out, they were a great deal closer than the Chancellor of the Exchequer.

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There was advice for the Chancellor from this side of the House too. Sadly, he neglected that. He told my hon. Friend the Member for Dunfermline, East (Mr. Brown), who presented a series of proposals for improving the situation, that there would be no change of policy. That was the Chancellor's absolutely unflinching announcement. He must have forgotten nine movements in the interest rate over a very short period, a kind of economic yo-yo, but he told my hon. Friend that there would be no change of policy. At all times, except when the Chancellor has faced the Prime Minister, his responses to demands and protests have been the same : "No change ; I am standing firm. Read my blips." That has been the answer he has offered this 12 months.

Let us hope there will be different responses in the forthcoming months ; otherwise there may be substance in the rumours percolating that the Prime Minister might be looking for a replacement for this Chancellor of the Exchequer. We understand that her gaze has fallen favourably upon the Secretary of State for the Environment. It is only a week since she was telling us that the right hon. Member for Cirencester and Tewkesbury (Mr. Ridley) is

"absolutely first-class in every way,"--*[Official Report, 7 March 1989 ; Vol. 148, c. 751.]*

whether in architecture, art, or civil engineering. Clearly, here we have a renaissance Cabinet Minister, with such an accumulation of talents as to make Leonardo da Vinci feel humble. So it might be that, in the course of the next 12 months, Michelangelo will replace Machiavelli. I do not know whether the country will be the better for it.

In this Budget the Chancellor did not offer anything to repair the damage done to ordinary families both as a result of last year's giddy, give-away Budget and so much else that the Chancellor of the Exchequer has been doing. His failure to make that reparation will dismay many people in our country, but it will not surprise them. Because, for instance, of the briefing that did not take place and the tapes that do not exist, the people of Britain now know that child benefit hangs by a mere comma in the Conservative Manifesto. They also know that they have a Chancellor who believes that only a "tiny minority" of pensioners have "difficulty in making ends meet", even though there are 6 million retired people in this country either below or just on the official poverty line.

So it comes as no surprise to the people of Britain that they have a Government who take with one hand and then take more with the other. They are a Government who give income tax cuts and then wipe out any gains with mortgage and interest rate rises and rises in other taxes, who have imposed the highest tax burden in peacetime history on the people of this country.

This Budget will not lessen the burden either on the family or on the national income. I see the Chancellor disagreeing. The fact is that, even to get back to the burden as a proportion of national income and a weight on the average family that was reached under the last Labour Government, the Chancellor would today have had to cut the standard rate of income tax by another 6p. That demonstrates how much of an increase there has been in the tax burden under this Chancellor of the Exchequer.

However, not content with maintaining that record tax burden, the Chancellor of the Exchequer has ensured that the greatest burden falls on the average family. Since the

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right hon. Gentleman, the great tax reformer, entered 11 Downing street, the bottom 50 per cent. of British taxpayers, over 10 million people, have received £10 billion in income tax cuts ; the top 1 per cent., just 200,000 people, have been given £16 billion in tax cuts. That cannot be just, efficient or right, and it will certainly not be right when that burden is increased by the Government-sponsored price rises in water and electricity and the poll tax- -no tax was ever conceived or designed to fall more heavily on ordinary families throughout the country and less heavily upon the very rich. Not content with being a high-tax party, the Conservative party, especially under the Prime Minister and the chancellorship of the right hon. Gentleman, is also spectacularly the high interest rate party. The average mortgage rate under this Government has been at an all-time record for an all-time record period. It is not an accident. The right hon. Gentleman told us last year, and he repeated it of course this year "that interest rates remain the"--

not "an" but "the"-- "essential instrument of monetary policy" *[Official Report, 15 March 1988 ; Vol. 129, c. 995.]*. While even he cannot have thought, when he said last year, that the essential instrument would become a 13.75 per cent. bludgeon on home buyers and a huge cost burden added to the costs of industry, it is only really this Chancellor's usual performance.

After all, in the past six years this miracle worker has raised the mortgage rate to a level more than 35 per cent. above that which he inherited. Today, just before he sat down, the Chancellor claimed that the changes in national insurance contributions make this a budget for the low- paid. They certainly need it, because the great supply-side reform that this Government has achieved is to remove both rights and protections for the lowest paid workers in the land. The right hon. Gentleman told us that he was going to claim credit for removing the steps in national insurance contributions. That is very interesting. We of course welcome it. We have made several demands over several Budgets for radical reform in national insurance contributions to alleviate the burden on the lowest paid workers. What has to be remembered, however, is that this man now removing the steps in national insurance contributions is the Chancellor who installed the steps in national insurance contributions and who increased the rate from 6.5 per cent. to 9 per cent.--a huge tax increase for those least able to afford it.

I wish this were a Budget for the low-paid. The truth is that the changes announced by the Chancellor today hardly touch the average family and its income, and they do not compare with the endless largesse that he was prepared to show last year to those on the very highest income. This is not a Budget for the low-paid worker ; this is another con job from a low-down Chancellor.

True to form, again in this Budget, while the right hon. Gentleman was failing the majority he was favouring the minority. Even this modest Budget today brought in a few more of what are becoming known as Lawson's loopholes. We have had them before. We had the BES and enterprise zones. Those are just two examples ; there are plenty more of them. We have had various kinds of tax relief, based on the hope that if the tax obligations of those on higher

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incomes were reduced they would be more willing to commit their resources to investment. That has never worked, and it will not work now.

The Chancellor has announced with a little twist today that, through this Budget, he will allow previously purchased privatisation share issues to be placed in personal equity plans. It will be plain to everyone that he is doing that to give free and speculative gains on privatisation issues. That is the water privatisation bribe, and the Government will need all the bribes that they can get if they are going to make that flotation work.

Of course, trying to relieve of tax the people on top incomes to induce them to invest has not worked. After 10 years of giving away £26 billion to the richest 1 per cent. in our country, the proportion of total investment in GDP is lower than during any year under the last Labour Government. The savings ratio is also at rock bottom. It is historically at its lowest ever figure.

I used to think that it was the national debt which did not matter. It now appears to be the savings ratio which does not matter. That is extraordinary. If the savings ratio does not matter, why did the Chancellor put all that effort into trying to subsidise savings if it was not to try to pull up savings from the historically low level which he has managed to reach as further evidence of his brilliance? The Chancellor's steps today, like so many of his other steps, show his incompetence and perversity. If the fact that we have 13 per cent. interest rates does not attract savers, why should subsidies attract them? In a country in which the Government refuse subsidies to meet the environmental costs of a rail link and in which they regard subsidies for training or research as the work of the devil, people rightly ask why subsidies are right for those with the money to save and wrong for those who use railways, carry out research or need training.

The Budget contains the most indefensible of all the Government's tax subsidies--the subsidy which they propose to give to people who buy private health insurance for the over-60s. If the Government want to give priority in the Budget to the health needs of the elderly, the answer is not tax relief on medical insurance premiums for the well-off. The answer is to provide proper funds to cut NHS waiting lists for the elderly, to increase district nursing, health visiting and chiropody and physiotherapy services. If the Prime Minister would only join the NHS queue instead of jumping it, she would know that I am telling the truth.

When I raised this matter with her, the Prime Minister said that she was surprised I was "prepared to purchase a private house but not prepared to purchase private health care. *[Official Report, 2 February 1989 ; Vol. 146, c. 424.]* That is what she said to me just a couple of weeks ago. The Prime Minister is so distant from reality that she equates housing with health. If she can do that, perhaps she can tell us what are the health equivalents to rent, mortgage arrears, housing, rises in mortgage rates, overcrowding and homelessness. If the Prime Minister believes that there is an equation between buying a house and buying private health insurance, she can tell us all about it. I might even get her to rise at the Dispatch Box to answer this, who knows?

The needs of the elderly, whether they are in the private sector or on the NHS, will not be met by subsidies of this kind. When we know that the Government, according to the Chancellor, are prepared to give over £40 million--it

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will be a lot more than that in reality--of taxpayers' money to the already well-off, when they are denying proper facilities to those who do not, cannot and will not pay, that is a grotesque sense of injustice.

We all know why that provision is in the Budget. It is not because the Chancellor is enthusiastic about it. It is not even, to do him credit, because the Secretary of State for Health is enthusiastic about it. That provision is in the Budget because it is one of the Prime Minister's pet obsessions. She deludes herself, or she wants to delude others, that private health subsidies for the over-60s will somehow ease pressure on the Health Service. It cannot and will not do that.

Apart from any other considerations, private health insurers do no cover pre-existing medical conditions such as arthritis, senile dementia, loss of mobility or many of the other most usual ailments of the very elderly. BUPA offers the advice that private health insurance does not exist to alleviate long-term illness, because that is not a suitable subject for insurers.

In the Finance Bill which will follow this Budget and in many other ways, it is important that people's attention is drawn to the basic ideology behind that proposition so that people can judge the Budget and the Government's White Paper on "Working for Accountants". The idea that the private medical sector can help with health needs is not the Prime Minister's only delusion. She believes, or says that she believes, that the

"trade deficit is being financed by people who are prepared to invest in Britain and who have full confidence in the country's economy."--*[Official Report, 2 March 1989, Vol. 148, c. 392.]* The Chancellor said something like that again today. However, the truth is that the brilliant Chancellor has made such a botch of his job that the only way in which he can get short-term money into this country to fund his record balance of payments deficit is to offer the highest interest rates in the industrial world.

At the same time that the Chancellor is making families and businesses bear the crushing interest rate burden, he is presiding over a huge and continuing net outflow of long-term capital. Last year, about £9 billion of long-term capital came into Britain and £24 billion of long -term capital went out. Some "full confidence" that shows in "the country's economy", to use the Prime Minister's words--a net long-term capital outflow of £15 billion to go with the deficit on the current account of £15 billion which will stay with us again this year.

However, against that background the Chancellor expects us to stand back and admire him for accumulating a Budget surplus. Against a background of huge household debt, a rock-bottom savings ratio, a massive trade deficit and a record tax burden, the Chancellor expects the people of Britain to become positively reverential at what he calls his "prudence and caution" in using that surplus to pay back the national debt.

Before anyone becomes too impressed with the Chancellor, a few factors should be taken into account. It is very difficult for the Chancellor to claim "prudence" for accumulating the surplus when he did not plan for it and when it is five times bigger than he expected. He was the most shocked man in the House of Commons. He must be the only person who still believes in Father Christmas. Despite all the talk that we heard again this afternoon about "prudence and caution" in paying off the national debt to "lift the burdens of the future", the Chancellor

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knows that he is not using the Budget surplus because he wants to. He is using it to repay the national debt because he thinks that he dare not do anything else with it.

The Chancellor has his bonanza budget surplus--a real windfall if there ever was one--which he believes that he cannot use in Britain without sucking in more imports and sending the markets haywire. He has all this money, but he dare not use it. He must feel like the robber who opens his swag and finds that all the banknotes are marked. The robber analogy is not entirely without meaning, especially when we bear in mind the remarks of the former Prime Minister, the late Lord Stockton, about selling the family silver. We must remember that the surplus is not the Chancellor's. The headlines might read "Mr. Lawson's surplus", "The Government's surplus", "The Chancellor's surplus", "Mr. Fixit's surplus", "Wonderman's surplus" or even "The Brilliant Chancellor's Surplus". However, as the Chancellor and the Prime Minister repeatedly and rightly remind everyone, Governments do not have their own money. Governments only have the people's money. Governments only have the taxpayers' money. So Governments do not have their own surpluses : they have only the people's surpluses.

What are the people in Britain saying should be done with their surplus? In every measure of opinion, such as that in The Daily Telegraph 10 days ago and confirmed by every other source, people are not saying that the surplus should be used to repay the national debt or to spend on big tax handouts. In huge majorities, in all measures of opinion, the people who own that surplus are saying that their surplus should be used on health, education, transport, to protect the environment and to make the streets and railways safer and cleaner. The people are saying that their surplus should be used to prepare for their future and for their children's future. That comes through strongly from every measure of opinion, and this is a day on which the Chancellor should have trusted the people. Some of the people want their surplus used in this way because of their instinct for social justice ; others because of an innate understanding that this country's economic and social fabric has been run down and must be built up if we are to face the future. But most people, I suspect, will say that their surplus should be used for constructive reasons of the most enlightened and common-sense self-interest, because the people of Britain know that they need the National Health Service and the public education system ; they need comfort and security and efficiency as they travel across the country. They know all that because, unlike the Prime Minister and most of the Cabinet, they use the public services in Great Britain. This is the time that the Chancellor really should have trusted the people of this country, because the National Health Service lacks the resources to spend properly on its development needs. In this country, rivers, beaches and water supplies need cleansing. In this country, under this Government, local council house building has dropped by two thirds, private house building has fallen by one third and we have increased overcrowding, bad housing and homelessness. Under this Government it is a country that spends a fraction of what our competitors spend on skill training and in which investment in commercially viable

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research is still, despite all the oil, the tax burden and the Budget surplus, still spending 10 per cent. less on research than in 1979.

In this country, with all those needs, the Government would have to spend £14 billion in order to raise the proportion of GDP spent on public sector capital investment back to the level it was at under the right hon. Member for Old Bexley and Sidcup (Mr. Heath), or under my right hon. Friends Lords Wilson and Callaghan.

The Chief Secretary to the Treasury (Mr. John Major) : He does not understand.

Mr. Kinnock : Oh, I understand only too well. One only has to walk out of this place and see the filth on the streets and the railways, the schools understaffed, the shortages of teachers and the under-funding of research to know that I understand only too well. In this country, with all these needs for repair and renovation and to face the future, a Government that use their Budget surplus to pay the national debt are like a householder who insists on paying back the mortgage despite the fact that the roof is leaking, the damp is rising, the electric wiring is perilous and the windows are falling out. This decision is justified by the Chancellor and the Prime Minister by saying that we should be paying off the mortgage, paying off the national debt, because if the people do not use their resources for that they will leave a debt round their children's necks.

It is strange that the Prime Minister and the Government as a whole always say that they do not want to leave debts to our children. Yet they are always prepared to cut the taxes of the rich and to restrain public capital spending. They do not want to leave debts to our children, but they are always willing to preside over stagnation in manufacturing investment, always ready to leave a legacy of decay and danger because they will not undertake proper investment in the present or the future.

They leave debts, too--the debts of a Chancellor who, in his time in office, has seen exports rise by 21 per cent. and imports by 58 per cent. In the last 12 months alone, he has seen exports rise by 1.8 per cent. and imports by 13 per cent. Such a Chancellor leaves debts. Such a Chancellor runs up overdrafts. Does he think that there is some charity in the sky that will fund that huge deficit that he has run up?

That is not all the debt story. Under this Chancellor personal debts have risen, because of his fiscal and monetary incompetence, to a level which means that British households are more indebted than those of any other of the seven major industrialised nations. The Chancellor, who now uses his single instrument of record interest rates, punishes people for believing him on previous occasions. This Chancellor and this Government allow decay to increase, danger to spread, debt to rise and division to increase. The people will have to pay those debts now because they are without choice when they face their bills. The right hon. Gentleman and the Government will pay later because they will have to face the people without support.

Mr. Speaker : As the private notice question is fully debatable on the Ways and Means resolutions, I do not propose to take any further questions on the private notice question.

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Provisional Collection of Taxes

Motion made, and Question put, pursuant to Standing Order No. 50 (Ways and Means motions).

That, pursuant to section 5 of the Provisional Collection of Taxes Act 1968, provisional statutory effect shall be given to the following motions :--

(a) Hydrocarbon oil (motion No. 2) ;

(b) Vehicles excise duty (rates) (motion No. 5) ;

(c) Special machines (vehicles excise duty and hydrocarbon oil) (motion No. 7).-- *[Mr. Lawson.]*

Question agreed to.