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Blind cc:- David Wright
(Cab. Office)

3 November, 1980

Corporation Tax: The Reform of Stock Relief

The Prime Minister has read the Chancellor's minute of 31 October on the above subject, and is content for you to issue a consultative paper on the basis proposed.

I am sending copies of this letter to Ian Ellison (Department of Industry), Stuart Hampson (Department of Trade) and to Robin Ibbs (CPRS).

J. E. LANKESTER

A J Wiggins, Esq
HM Treasury



Prime Minister
Content that the
Treasury ~~will~~ should
issue a consultation
paper?

Treasury Chambers, Parliament Street, SW1P 3AG
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(on the form of
it, the proposals
look very
smooth.)

PRIME MINISTER

Yes
not.

CORPORATION TAX: THE REFORM OF STOCK RELIEF

As you know, Arthur Cockfield has been working with my officials on the much needed reform of the present rules for stock relief.

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2. We have now reached the point where we are ready to bring forward our proposals for the consultation with outside industry and the accountancy profession, which I promised in my Budget Statement last March.

3. I do not think that I need to trouble you with the details at this stage. The main objectives of the new scheme will be:

i. To place the stock relief on a more rational basis, by adjusting taxable profits much more precisely by reference to the effects of inflation on the holding of stock; and thus to move, even if tentatively, in the direction indicated by the new accounting standard SSAP16.

ii. To reduce the present incentive for a company artificially to build up its level of stocks, simply for the sake of a tax advantage.

iii. To remove the damaging effects of stock relief recovery (or "clawback"), when companies reduce their stocks - for example, in an attempt to ease

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liquidity problems in the current recession.

iv. To deny relief, to the extent that stocks are financed by credit or other borrowing.

4. A scheme on these lines would effectively deal with the abuses of the present stock relief, but the restructuring would in present circumstances have the additional advantage of giving more relief for business as a whole, and in particular for manufacturing industry. Depending on the eventual details of the changes, there could perhaps be something of the order of £2-300m extra injected into the business sector in 1981/82, and this obviously has certain implications for my 1981 Budget. However, I believe that this is something to which it is right to give a high priority, given the present pressures on business profits and liquidity. And these proposals go a long way - much more effectively than other proposals we have had from, for example, the CBI - to give most help where it is most needed.

5. My officials have kept their opposite numbers in other departments informed about the general nature of the reforms which we have been considering; and have now circulated in the official consultative group a full series of papers, which set out our detailed proposals, as they now stand, the reasons for them and our best estimates of their effects on the yield and incidence of tax.

6. If you and other colleagues are content, the next step will be to issue the consultative paper. This will need to be done quite soon, if we are to give industry and the accountancy profession reasonable time to consider our proposals, and be ready for legislation in the 1981 Finance Bill. The scheme is complex and the paper will need



careful presentation. Some points in it will be controversial, and there are bound - both because of the credit restriction and other changes - to be losers as well as gainers. I will of course consult interested colleagues again.

I am sending copies of this minute to the Secretaries of State for Industry and Trade and to Robin Ibbs.

(G.H.)

3/ October 1980