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CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
Financial Secretary
Minister of State (C)
Mr Ridley
Mr Cropper
Mr Cardona

1981 BUDGET

1. PSBR

With an 11% rate of inflation and a 1½% fall in GDP a percentage next year the same as this year would mean a rise in the money figure from £11½bn to say £12½ bn.

To keep the money figure unchanged would mean a reduction in percentage from about 5% to about 4½%. This would still be well above this year's target as given in the MTFS. I would regard it as the minimum we ought to aim for. I would like to go lower but doubt the practicability of so doing particularly having regard to the fact that I do not think the economy will turn up as quickly as many commentators are suggesting.

2. Revenue

The question is not whether it is "felt" but whether it is needed. We really need to have some indication of the size of the gap to be bridged

- (a) My prime candidate - the NIC - has now been adopted
- (b) I would in principle increase the specific duties sharply but declining returns on alcohol and tobacco may impose a severe limit. I am less worried about the RPI effects now that inflation is on a downward path. This may be our last real opportunity.

- (c) I would try and avoid de-indexing the tax thresholds if at all possible but whatever we do we should treat all thresholds alike.
- (d) Presumably input blocking for petrol is still on the cards.

Apart from this, the nub of the problem is the increasing ineffectiveness of the tax system. There are clearly very large sectors of the economy that by one device or another are slipping through the tax net. In the Corporation tax field people like the Banks who ought to be paying a great deal are paying virtually nothing because of various forms of tax sheltering.

3. The "Burns-Middleton" analysis at least in the form it is summarised in the questionnarire, suffers from the fallacy of composition. We need to find some means of lightening the burden on the unfortunate without lightening it on the fortunate. This is the point made under (d) above. It is very difficult to introduce this kind of discrimination into the tax sphere. Possibly we shouldn't have abolished the SET - which was discriminating in a way that the NI Surcharge isn't.

4. (i) I believe we must do something on the capital taxes even at the risk of pleasing our supporters. I would think the absolute bed rock minimum would be to index thresholds and bands in line with what we do on the income tax. If we never start we never will. But I hope we will do more.

(ii) I see no reason for reducing the NIS unless it were done in the context of what I have said under 3 above. I wouldn't mind increasing the rate on finance, commerce and distribution in return for reducing the rate on industry, possibly making a profit for the Exchequer en route.

A.C.

LORD COCKFIELD

16 December 1980