

cc A Duguid
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PRIME MINISTER

TAX AND PUBLIC EXPENDITURE - THE NEXT STEPS

Following our discussion in Cabinet on 17 June I have been considering how we should carry forward decision-making in the tax and public expenditure field, with particular reference to the discussion in Cabinet due to take place on 23 July.

2. We agreed on 17 June that we should in the context of the forthcoming Public Expenditure Survey round consider the balance to be struck between the Government's taxation and public expenditure objectives, and the balance, within the public expenditure programme, between capital and current expenditure.

3. Economic prospects may alter between July and October, so I may not want to be too precise on 23 July. What I have in mind for that discussion, therefore is to put before our colleagues one or possibly more "packages" which would illustrate what the trade-offs might be between specific objectives for the tax burden on the one hand, and public expenditure on the other. These calculations would of course assume that the medium term financial strategy holds, but they might make alternative assumptions about the precise developments in the economy given our overall approach to policy. So far as tax goes, they might explore the implications of alternative assumptions about where any tax relief (over and above normal revalorisation) might be given - eg all to companies, or in part to companies and in part to persons.

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4. The other side of this coin is public expenditure. I should at the least want to discuss in my paper for 23 July the preliminary prospects for public expenditure as they are emerging from the Survey, and as they would need to be in the light of the alternative tax strategies presented. This would cover the sort of reductions that might have to be found, and the general sort of areas in which they might be found, if we had to accommodate the additional bids that we expect (notably in respect of nationalised industries), perhaps find some additional money in areas to which colleagues attach particular importance (eg alleviating youth unemployment and may be some more capital expenditure) and still make what necessary overall reductions would be required to meet the tax strategies. The years considered would be 1982-83 through to 1984-85 - the Survey period.

5. My objective on 23 July would be, therefore, to secure colleagues' general agreement, on the basis of a given tax strategy or strategies, to a general view of the sort of reductions from the plans implied in Cmnd 8175, with some ideas as to where these reductions might - or alternatively might not - be found.

6. This would be preparatory to our autumn discussions. As you know we are to consider in Cabinet on 15 September what revision if any might be made to the factors provisionally adopted for translating the Cmnd 8175 public expenditure figures into cash, and we are to consider on 20 October my detailed proposals in respect of public expenditure. The discussion on 23 July is intended to guide me to what I shall propose on 20 October. But I have been considering how, from the point of view of mechanics, we might bring discussion subsequent to 20 October to agreement. Over the last 2½ years we have seen how even when our colleagues have agreed on overall targets or objectives we have had the utmost difficulty in securing the necessary detailed decisions on programmes to get to those totals. We may need a different



approach.

7. I have not come to any final view yet. But depending on the sort of decisions which appear to be necessary and how difficult these are likely to be, I may want to suggest that we should try again, but with some changes, the use of a small group of Ministers charged with implementing Cabinet's decisions. Such a group might comprise Treasury Ministers, some big spending Ministers, and some "non-economic" Ministers. The important thing, however, is that it would be made clear to all our colleagues and to the group, that the group was intended to settle matters. The problem in the past is that spending Ministers have been able, often with success, to appeal to full Cabinet, which undermines the work of such a group. (I should make it clear that such a group would not necessarily completely replace the usual bilateral discussions between spending Ministers and Treasury Ministers; where such bilaterals are likely to be useful - before or after 20 October - I hope they would continue).

8. As I say there is no need to take any decision on this yet. Such a group could not really set to work until after 20 October when I have made my specific proposals - though I would not rule out the possibility of it meeting some time between 15 September and 20 October to consider those proposals. When it does get down to business, however, it will have to conclude its work early in November, in order to enable Cabinet to decide any residual disagreements - in theory there should be none - on 5th or 12th November so as to meet our general timetable.

9. This of course is only a general outline of how I propose to proceed, and there are details yet to be considered. But I hope you will agree to this general way of going forward.

A handwritten signature in dark ink, appearing to be 'G.H.' with a flourish.

(G.H.)
25th June 1981