for e K Soles

eJV

(2)

Prime Minister

Support for Mr Prior.

MCS 6/9

CONFIDENTIAL

Qa 06054

To: PRIME MINISTER

From: JOHN SPARROW

6 September 1982

Industrial Incentives in Northern Ireland

1. The memorandum by the Secretary of State for Northern Ireland shows that the prospects for the economy and for jobs in the province are extremely gloomy. A fundamental improvement is required in the performance of the Northern Ireland economy. At present, it suffers from a legacy of weak traditional industries (like shipbuilding), low productivity, uncompetitive wage levels and an excessive dependence on public sector employment. The measures proposed by the Secretary of State should begin to move the economy in the right direction.

2. A number of the proposals will reduce the bias in the present package of industrial incentives towards subsidising capital as against labour. Such changes should encourage more profitable labour-using investment, and hence generate more jobs efficiently (a theme in our unemployment report, likely to be followed up in the Quinlan review of GB regional policy). Both major proposals are of this type:

- A reduction in the National Insurance Surcharge for Northern Ireland would inject a regional dimension in what has hitherto been a uniform tax. The unique circumstances of Northern Ireland mean that it need not be viewed as a precedent; the Quinlan review will be examining whether there is a case for regional differentiation of such taxes in the rest of the United Kingdom.

- The proposed Corporation Tax Relief Grant has a number of attractive features, in particular the fact that it will act as a reward for success. Thus while it may not increase the total investment in Northern Ireland, it should help to increase its quality. The CPRS supports its introduction.

There are of course still technical problems with the proposal, for example companies may seek to boost artificially their profits in Northern Ireland in order to gain tax advantages, but officials should be asked to tackle these when working out the details of the scheme.

3. Clearly the Secretary of State is right in saying that the public expenditure implications for the late 1980s can only be highly speculative, in such uncertain circumstances. Nevertheless there is one principle worth noting: if savings are needed at a later date, they should be found by means of a reduction in the rate of the Standard Capital Grant - as the officials' report points out, this would be consistent with the strategy of shifting the balance from capital to labour subsidies.

4. Reducing labour costs by exerting pressure on wages in the Province is also supported by the Secretary of State. The officials' report makes a number of specific suggestions about how this might be done (para 2.35), although it points out that there would be merit in applying most of the measures throughout the United Kingdom. The Secretary of State points out that this will be a highly sensitive issue (although less so if it is done less overtly) and wishes to consider it further. He might be asked to report back on the results of his further consideration at the same time as he presents a detailed scheme for a Corporation Tax Relief Grant.

5. I am sending a copy of this minute to Sir Robert Armstrong.

JB.