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A review for the Treasury, J

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22 Feb 82

Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Patrick Jenkin MP
 Secretary of State
 Department of Industry
 Ashdown House
 123 Victoria Street
 London SW1E 6RB

22 February 1982

REGIONAL DEVELOPMENT GRANTS

I am writing to let you and colleagues know that I have decided not to press for the cuts in expenditure on RDGs which were agreed by Cabinet in connection with last year's survey. I continue to find it very disappointing that you and others have been unable to agree on a way to fulfill your commitments on finding the savings, especially since everyone seems to support the view that a considerable part of this expenditure is wasted on large capital-intensive projects providing very few jobs. This I feel is certainly something which must be tackled in any longer-term review of regional policy and regional incentives, but we shall in any event need to return to the issue at an early date.

The baseline for your programme for 1983-84 and 1984-85 will remain at the level agreed by Cabinet, including the £50 million saving on RDGs. If you cannot find alternative savings or reduced requirements you will have to put in a bid in next year's survey, which will of course be considered in the ordinary way. For 1982-83 I propose to leave your estimate at the level proposed, with the £30 million reduction. If later in the year it appears that expenditure on RDGs will exceed this estimate you will have to put in a supplementary: I shall not now press for administrative action, or for an increase in deferment.

Although I am, with reluctance, prepared not to press the case for any general savings on RDG there is one point on which we must act. You will recall from our discussions of Sullom Voe and Flotta last autumn that onshore oil and gas production facilities qualifying both for RDGs and for PRT and Corporation Tax relief can attract total exchequer support (tax relief plus RDG) well in excess of gross spending. Despite our decision on past expenditure, we were agreed that this should be stopped for the future (E(81)33rd meeting). Now that we are not proceeding with the proposals to exclude all large capital projects we need specific measures to deal with expenditure which falls within the oil tax "ring-fence".

The most straight-forward course would be to ensure that RDGs were never given in such cases. You yourself suggested last year that the scope of RDGs might be limited to exclude "oil terminals." If this could be done to exclude all future expenditure likely to qualify for PRT relief, that would seem to me to be the best answer. But I understand that officials have found difficulty in drawing a new line in exactly the right place, and perhaps you could confirm that that is so.

On that basis I am bound to propose legislation in this year's Finance Bill to net off RDGs against future expenditure for the purpose of relief against both PRT and "ring-fence" Corporation Tax. The position for past expenditure is bad enough (although it must be regarded as water under the bridge); but I do not see how we can allow the excessive allowances which arise from combining RDG and the tax allowances to continue in the future.

For the immediate future I believe that the only major project known to be involved is the Shell/Esso gas fractionator (not the cracker) at Mossmorran. I recognise the special position of the cracker there, but I do not favour any transitional provisions to let out RDGs on money not yet spent on the fractionator. We are already facing considerable criticism on our commitment to legislation on ethane valuation.

You will appreciate that the timetable for Finance Bill legislation is now very tight: I am afraid that I need definite confirmation by the middle of this week that tax legislation is needed to deal with this problem.

I am copying this letter to the Prime Minister, the Secretaries of State for Scotland, Wales and Energy and to Sir Robert Armstrong and Mr Ibbs.

LEON BRITAN

22 FEB 1982





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Secretary of State for Industry

24 February 1982

The Rt Hon Leon Brittan QC MP
Chief Secretary
Treasury
Parliament Street
London SW1

From: Minister's Sec

AW
24/2

Dear Chief Secretary

REGIONAL DEVELOPMENT GRANTS

Thank you for your letter of 22 February.

2 I agree that regional incentives for large capital-intensive projects need to be made more cost-effective and this will be tackled in any longer term review of regional policy.

3 I appreciate that the estimates for the Department's programme for 1983-84 and 1985-86 must remain at the level agreed by the Cabinet. But as things are the reduced figures are unlikely to be sufficient and the possibility of a supplementary for 1982-83 cannot be ruled out.

4 Turning now to your proposals for ring-fence expenditure, I must confirm that it is not practicable to exclude from grant expenditure qualifying for PRT relief. But I agree something has to be done to reduce the incentives and I would be happy for officials to discuss this further.

5 I note what you say about Mossmorran. However, we concluded earlier that any reduction in RDGs on the fractionator ran the risk of damaging prospects for the cracker. Your proposal in effect could mean that RDGs were not worth claiming in respect of the fractionator. I understand that a considerable part of the expenditure has yet to be committed and without any transitional provisions Shell/Esso could be badly hit. In view of the risks involved, I should prefer some transitional relief for the Mossmorran fractionator especially as we know of no other cases that would benefit. If no transition were allowed and the possibility of offsetting selective assistance had to be considered, the tax problem would come up again because SFA is taxable.



6 I appreciate the need to move quickly on this, but I would ask for a little time so that officials from the interested Departments can meet to gauge the impact of your proposals, particularly on the Mossmorran project where they will need also to assess the risks involved.

7 I am copying this letter to the Prime Minister, the Secretaries of State for Scotland, Wales and Energy and to Sir Robert Armstrong and Robin Ibbs.

Yours sincerely

Richard Riley

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(approved by the Secretary of
State and signed in his
absence)