ECNO

Prime Minister (2)

This argument will no doubt recur

AT 4/7

SECRETARY OF STATE FOR ENERGY
THAMES HOUSE SOUTH
MILLBANK LONDON SW1P 4QJ

CONFIDENTIAL 211 6402

The Rt Hon Peter Rees QC MP
Chief Secretary
H M Treasury
Parliament Street
London SW1P 3AG

3 July 1984

Dear Peter

IFR: CORPORATION TAX

Following the discussion in E(A) this morning I should like to clear up the slight misunderstanding which arose over the impact of Corporation Tax.

The figure which I was quoting were for total increases in the energy industries' Corporation Tax payments since last year's IFR. The figures which you were quoting were for changes attributable to the Budget. The difference is significant:

	1985-86	1986-87
Increases in Corporation Tax payments since the last IFR	75	412
Increases attributable to the Budget	33	249

The effect is even more marked in 1987-88 (which was not of course part of last year's IFR). Extra payments of Corporation Tax by the energy industries are forecast to rise to £850 million in that year, compared with previous levels.

The point I was making was that adjusting the baselines of the energy industries to accommodate these extra payments - whether attributable to the Budget or not - would make absolutely no difference to the PSBR, as the paper by officials acknowledged. The Exchequer would just get the money in the shape of tax revenue rather than repayment of debt or deposits of surplus cash.

CONFIDENTIAL

So far as the Budget is concerned, the Exchequer would in effect be raising the money twice if the industries were forced to absorb the higher tax within unchanged EFLs. My understanding is that adjusting the EFLs would be consistent with the Budget judgement. Anything less would mean a tighter fiscal stance than the Chancellor intended.

I appreciate your point about private sector companies having to absorb the extra tax. But any private sector company faced with the situation of these industries would explore ways of minimising its tax burden (in this case, possibly by bringing forward investment) or consider options such as cutting dividends or increasing borrowing which are not open to nationalised industries. It is not a genuine parallel.

No doubt we can pursue these points in the Autumn when we come to the bilaterals. I just wanted to make sure we were not at cross purposes.

I am copying this to other members of E(A) and to Sir Robert Armstrong.

Peter

PETER WALKER

CONFIDENTIAL

CC/SO

SECRETARY OF STATE FOR ENERGY
THAMES HOUSE SOUTH

NBPM

AT 20/7

01 211 6402

The Rt Hon Peter Rees QC MP
Chief Secretary
HM Treasury
Parliament Street
LONDON
SW1P 3AG

19 July 1984

Dear Peter

IFR: CORPORATION TAX

Thank you for your letter of 10 July. It goes without saying that I shall be doing my best, in discussions with my industries, to secure necessary savings. But we must recognise that one of the effects of the Budget has been to make all capital intensive industries - whether in the public sector or the private, including those which I sponsor - less profitable to their proprietors. And we cannot ignore the fact that to press industries to achieve savings to "compensate" for having to pay extra tax tightens the PSBR beyond what was intended in the Budget. This Corporation Tax question cannot be dismissed, it is a central issue of the IFR.

I am copying this letter to E(A) colleagues and to Sir Robert Armstrong.

Peter

PETER WALKER

CONFIDENTIAL

Econ Pol Pt 13

Budget

CC NO

NBPM

AT 11/7

CHIEF SECRETARY TO THE TREASURY

Treasury Chambers, Parliament Street, SW1P 3AG

Rt Hon Peter Walker MBE MP
Secretary of State for Energy
Department of Energy
Thames House South
Millbank
LONDON
SW1P 4QJ

10 July 1984

Dear Peter

IFR: CORPORATION TAX

Thank you for your letter of 3 July. I am quite happy with the figures you quote. - with AT?

You go on to make some points about the ways private sector firms might respond to extra tax liabilities. I would point out that there are very real practical limits on the extent to which companies can bring forward investment. This point has in fact been made recently by a number of companies. As far as cutting dividends is concerned, this is, as you will appreciate, far from a costless option. Company managers are usually reluctant to cut dividends as it raises the cost of new equity funds and also increases vulnerability to take over.

You say we can return to this in the bilaterals. However, as you appreciate their purpose is to identify the savings needed to achieve the reduction in public expenditure agreed in E(A). This will not be an easy task in any event and I hope therefore we can concentrate on that rather than spend much time on the Corporation Tax question.

I am copying to other members of E(A) and to Sir Robert Armstrong.

Yours ever
Peter

PETER REES

17 JUL 1984