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Prime Minister

See also

CPRS brief

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Ref. A0923

PRIME MINISTER

Enterprise Proposals

(E(79) 77, 82 and 83)

BACKGROUND

The Chancellor of the Exchequer's paper (E(79) 77) deals with 12 proposals for action "to encourage enterprise and the growth of the small firms sector" (these "enterprise proposals" are not related to "enterprise zones"). The Chancellor proposes to implement five of the schemes, accept another one in principle, and remit two more for further study. He rejects the remaining four. The CPRS (E(79) 82) suggests that one of the Chancellor's "favoured five" should be left out (a reduction in the "small firms rate" of Corporation Tax). Unlike the Chancellor, however, the CPRS does not want to turn down out of hand the "start-up scheme", although it involves further tax relief for individuals. The Secretary of State for Industry (E(79) 83) wants the "start-up scheme" introduced at once. The Secretary of State for the Environment has not circulated a separate paper, but can be expected to resist strongly the Chancellor's proposal to turn down his own two proposals ("Transfer of Investment Allowances" and "Investment Rebate Scheme"). There were signs in earlier discussions that his readiness to accept further cuts in his public expenditure programme would be conditional on his colleagues' acceptance of these proposals. !

2. It would have been helpful, time allowing, for the Ministers directly concerned to meet and sort out their differences. This may still be the best solution. We have left the paper on the agenda, so that the Committee can have a first run over the problems. If the Chancellor is right in his cautious approach, there is no need for immediate decisions: these matters can be left till the Budget. But I think you had hoped for at least "a small firms" package which could be announced very early. This would still be possible, but only if the first four (or five) bits of the package are announced in advance of the rest. An early decision on these items would be needed if there were to be an announcement in the New Year.

3. As with the earlier paper on profit sharing (E(79) 76, Item 2 on this agenda) everything turns on how much the Chancellor can afford in the next Budget. Assuming Cabinet approves the reopening of public expenditure totals, there could be a little room for manoeuvre: indeed, introduction of an "enterprise package" of some kind might make the expenditure cuts more palatable. It would also require them to be bigger. Ministers have therefore got a choice to make, and it will not be easy to take a final view until after the Cabinet discussion on public expenditure on Thursday.

4. The merits and demerits of the different schemes are set out in the various papers. The best course is probably to go through them one by one.

#### HANDLING

5. You might therefore call for an opening statement from the Chancellor of the Exchequer, and thereafter take the Committee through the various schemes, following the sequence in the Chancellor's covering paper (paragraph 4 onward):

- (i) Abolish the rules for apportioning the trading income of "close" companies.  
No objections likely.
- (ii) More generous tax relief for self-employed people who take out retirement annuities. No objections likely.
- (iii) A reduction in the rate of Corporation Tax for small companies, from 42 per cent to 40 per cent. The Chancellor is prepared to recommend this: the CPRS argue that it is not cost-effective, although legislatively easy (even this is not certain: it will require a workable definition of a "small firm" which could be difficult to find). The Secretary of State for Industry is likely to support the Chancellor strongly.
- (iv) Widening tax relief for interest on the loans for investment in closely controlled companies. No objections likely.
- (v) A new relief from stamp duty to assist the marketing of unlisted companies.  
No objections likely.
- (vi) The "Losses scheme". There is a full description of this in paragraphs 2.6-2.10 of the interdepartmental report. The Chancellor does not turn it down flat: he proposes it for further study. The Secretary of State for Industry argues against it, as less cost-effective,

# CONFIDENTIAL

and psychologically more damaging, than his preferred option, the "Start-up scheme". The CPRS argues for the "Losses scheme" but draws attention to the administrative complications.

- (vii) The Equity Investment or "Start-up" scheme. For the details, see the interdepartmental report on "Tax Relief for New Investment in the Equity of Small Firms". The scheme would work by giving individuals tax relief on income which they spend on buying shares in new ventures. There would be many problems of definition, and a very serious problem of evasion. The cost might therefore be high. But it is a gambler's risk: the pay-off could also be very large, if it led to new ventures on a substantial scale. It is much the biggest of the schemes. The CPRS paper goes into the problems in more detail (paragraphs 5-8). Its cost probably rules it out for the 1980 Budget anyway. Are Ministers content that it should be studied meanwhile?
- (viii) Small Firms Investment Company. This is a proposal (paragraphs 2.16-2.18 in the official report) for filling the "Equity gap". There is no dissent from the Chancellor's proposal to study it further.
- (ix) Relief from VAT on bad debts. Similarly, a review can be put in hand quickly: but there is no prospect of immediate action.
- (x) A tax holiday for new businesses. This was Sir Keith Joseph's main proposal. It has analogies with the "enterprise zone" proposals which will be before the Committee next week, though it has proved impossible to find a way of introducing "tax holidays" on a geographically selective basis. The main difficulty, however, lies with the self-employed. The Secretary of State for Industry did not propose that they should be exempt: yet there is no easy way of keeping them out if they decide to incorporate themselves. The Chancellor recommends rejection. Does the Secretary of State, on reflection, agree?
- (xi) An Investment Rebate Scheme. This, and the next one, are the two "accelerator" proposals for "encouraging winners" put forward by the Secretary of State for the Environment. He has never reduced them to writing, but has briefed his officials who have had several discussions

with the Inland Revenue. Neither scheme seems a starter.  
Paragraphs 3.6-3.11 of the interdepartmental report explain why the Investment Rebate Scheme is not favoured. The original idea of tax rebates will not work anyway, because many taxpayers would not have the necessary liabilities against which to offset the very generous allowances. The scheme is therefore a "grants" scheme. As such, it is just another version of investment incentives, directed at companies which already have a proven track record. The Chancellor rejects it simply on its public expenditure cost. The CPRS have also studied the proposal (although it is not covered in their paper) and I believe that they too advise against it (Sir Kenneth Berrill to comment?).

- (xii) Transfer of Investment Allowances. Paragraphs 3.2-3.5 of the inter-departmental report deal with the second of Mr. Heseltine's proposals. The Chancellor rejects it on grounds of principle. It involves making a company's additional tax allowances available to its shareholders. It is very much more open to tax avoidance than the "start-up" scheme. The Chancellor recommends rejection. Does the Secretary of State for the Environment acquiesce?

#### TIMING

6. At this point, you will want to consider whether there is enough of a package available to justify an early announcement. The Chancellor's proposals would cover only items (i)-(v) above (and the CPRS object to (iii)). He also suggests that (vi) could be considered for the 1980 Budget. Is he, therefore, ready to announce some or all of items (i)-(v) before then? Is this a sufficiently large package to be credible, or would it be better to wait for the Budget?

#### CONCLUSIONS

7. You will want to record a view for or against each of the 12 items listed above. You could then leave the Chancellor to decide which of the favoured items he could afford in the 1980 Budget - or alternatively which can be afforded and announced earlier in a separate package.

RAA

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