CONFIDENTIAL

THIS DOCUMENT IS THE PROPERTY OF HER BRITANNIC MAJESTY'S GOVERNMENT

E(80) 39th Meeting

COPY NO 55

CABINET

MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

MINUTES of a Meeting held in the Prime Minister's Room, House of Commons on WEDNESDAY 5 NOVEMBER 1980 at 3.00 pm

PRESENT

The Rt Hon Margaret Thatcher MP
Prime Minister

The Rt Hon William Whitelaw MP
Secretary of State for the Home Department

The Rt Hon Lord Carrington
Secretary of State for Foreign and Commonwealth Affairs

The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer

The Rt Hon Sir Keith Joseph MP
Secretary of State for Industry

The Rt Hon Lord Soames
Lord President of the Council

The Rt Hon James Prior MP
Secretary of State for Employment

The Rt Hon Peter Walker MP
Minister of Agriculture, Fisheries and Food

The Rt Hon Michael Heseltine MP
Secretary of State for the Environment

The Rt Hon John Nott MP
Secretary of State for Trade

The Rt Hon David Howell MP
Secretary of State for Energy

The Rt Hon John Biffen MP
Chief Secretary, Treasury

THE FOLLOWING WERE ALSO PRESENT

The Rt Hon George Younger MP
Secretary of State for Scotland
(Items 2 and 3)

The Rt Hon Nicholas Edwards MP
Secretary of State for Wales
(Items 2 and 3)

The Rt Hon Humphrey Atkins MP
Secretary of State for Northern Ireland
(Items 2 and 3)

The Rt Hon Sir Michael Havers QC MP
Attorney General
(Item 1)

The Rt Hon Norman Fowler MP
Minister of Transport
(Items 2 and 3)

Mr J R Ibbs
Central Policy Review Staff

SECRETARIAT

Sir Robert Armstrong
Mr P Le Cheminant
Mr D J L Moore (Items 2 and 3)
Mr G D Miles (Item 1)

CONFIDENTIAL

CONTENTS

1. COMPUTERISATION OF PAY AS YOU EARN

Previous reference: E(80)31st Meeting, Item 1

The Committee considered memoranda by the Chancellor of the Exchequer (E(80) 123) and the Lord President of the Council (E(80) 124) setting out new proposals for the computerisation of the Pay As You Earn (PAYE) tax system. The Committee also had before them letters from the Paymaster General to the Lord President and from the Secretary of State for Industry to the Lord President, both dated 4 November, commenting on aspects of these proposals.

THE LORD PRESIDENT said that the new proposals simplified the system, by cutting out the direct links between regional computer centres. He was advised that the new system would still meet the operational requirement, and was within the competence of International Computers Limited (ICL), although it was likely that, because they would be using new equipment, a system provided by them would come into operation rather later than a system provided by one of the competing companies. If the Government wished to award a contract to this company on single tender, it would be necessary to reach a binding contract before the end of the year, since from 1981 the contract would have to be offered in open competition under the terms of a European Community (EC) Directive. This short timescale would make the process of contract negotiation difficult, but the hand of the Government negotiators would be strengthened if an announcement of the Governments intention could be deferred until the contract was ready for signature.

THE CHANCELLOR OF THE EXCHEQUER said that the cost penalty arising from delayed implementation of the new system would amount to £46 million per year. He continued to have misgivings about the technical competence of ICL for a task of this magnitude, particularly since untried equipment was involved.

THE ATTORNEY GENERAL advised the Committee that the terms of the EC Directive requiring open competition would not apply to this contract, provided that Heads of Agreement had been signed before the end of the year. The detail of the contract could follow later. He would not favour trying to go into more detail than general Heads of Agreement before the end of the year.

In discussion the following main points were made -

a. The figures in the assessment attached to the paper E(80) 124 were not a true reflection of the cost of the project. When allowance was made for ICL's standard pricing policies there was likely to be very little difference in the price levels of ICL and the competing companies.

b. Although there was anecdotal evidence of unreliability from ICL computers, it was not evident that these reflected a worse level of service than that of other companies. ICL had greatly improved its performance in recent years, and was competing successfully, without preference, in many parts of the world.

c. The contract negotiations with ICL should be tough, to ensure that the interests of the taxpayer were protected. This need not imply that public uncertainty about ICL should continue until the detail of the contract was finalised, since once Heads of Agreement were signed ICL would know that a failure on their part would have disastrous consequences for confidence in the company, and for their other business.

d. It was desirable that the contract should include provision for breakpoints if ICL failed to meet the required specifications and the system should be so designed that alternative equipment provided by other manufacturers could if necessary be substituted for ICL equipment. This would probably imply the adoption of international standards. ICL should also be asked to accept the obligation to provide additional equipment without charge, if this proved necessary as a result of failure of their new computers to reach the specified performance levels.

e. The delay in placing a contract had already shaken world confidence in ICL, and it was desirable that the uncertainty should be ended as soon as possible. ICL would recognise the importance of making a success of this project to their company's image and the Government should not weaken the impact of placing this major contract with a British company by an appearance of grudging support.

THE PRIME MINISTER, summing up the discussion, said that the Committee were agreed that computerisation of PAYE should proceed on the basis of the system now proposed. The contract should be offered to ICL on single tender. Heads of Agreement should be settled and signed as soon as possible, and in any case before the end of the year. They should be followed by a firm negotiation on the detail of the contract, with the aims of achieving provision for breakpoints, of retaining the possibility of using alternative equipment, and of placing on ICL the onus of providing additional equipment free of charge if necessary, as had been suggested in the discussion. The Lord President, in consultation with the Attorney General and the head of the CPRS, should arrange to draw up suitable draft Heads of Agreement as soon as possible. When these were available, and had been seen by interested colleagues, the best method of approaching ICL with them, and the form and content of a public announcement, could be further considered. The Committee noted that the accommodation for these computers would be a competitor with other Departmental requirements for a share of the Property Services Agency budget for new works.

The Committee -

1. Agreed that the contract for the computerisation of the Pay As You Earn system should be offered as a single tender basis to International Computers Limited.

2. Invited the Lord President, in consultation with the Attorney General, and the Head of the Central Policy Review Staff, to draw up suitable Heads of Agreement.

3. Agreed that the method of approaching International Computers Limited and the type of public announcement should be considered further when draft Heads of Agreement were available.

4. Agreed that subsequent detailed negotiations with International Computers Limited should be conducted toughly, with a view to securing the conditions suggested in discussion, to ensuring prompt and efficient performance by International Computers Limited, and to obtaining the best possible value for the taxpayers' money.

CONFIDENTIAL

2. NATIONALISED INDUSTRIES: EXTERNAL FINANCING LIMITS 1981-82

Previous Reference: E(80) 38th Meeting, Item 2

The Committee considered memoranda by the Chief Secretary, Treasury (E(80) 121 and 125) on the External Fianacing Limits (EFLs) of the nationalised industries in 1981-82.

THE CHIEF SECRETARY, TREASURY, said that, following further discussions between sponsor Ministers and their nationalised industries, the EFLs now proposed were £757 million higher at 1980 survey prices than the base-line agreed in July; and £457 million higher than the additional provision of £300 million which was assumed in the public expenditure proposals now under discussion by the Cabinet. There were particular difficulties over the EFLs of the British Gas Corporation, the Electricity Council and Boards, British Rail and, to a lesser extent, the British Airports Authority. In view of the failure to reach agreement on further cuts in particular industries he was no alternative but to recommend across the board cuts yielding £457 million, equivalent to 9 per cent of the proposed level of fixed investments in the Investment and Financing Review attached to E(80) 64. Although these cuts would be calculated by reference to investment programmes he stressed that they would not necessarily be made on investment. It would be for each industry to decide how to achieve them and, so far as possible, the emphasis should clearly be on reducing current costs, especially pay.

In discussion the following points were made -

a. It would be very difficult to make cuts of the scale required without either higher tariff increases - particularly for Gas, Electricity and Rail - than sponsor Ministers and their industries judged to be defensible, or yet further cuts in investment on top of those already being made. Either course would be highly damaging to the private sector generally, and (in the case of cuts in investment) to the supplying industries in particular. In the case of British Rail cuts on investment would inevitably fall heavily on rural services.

b. On the other hand, failure to make the savings required would be even more damaging to the private sector if it led to higher taxation or to higher borrowing and, in turn, yet higher interest and exchange rates. The right course was to make the cuts but to find them as far as was practicable, from further privatisation and from reductions in running costs, from lower wage settlements and from staff savings. The best stimulus to greater efficiency in the nationalised industries was to increase their exposure to competition.

c. There was still scope for adopting more realistic pay assumptions for some of the industries; and, in particular, it was agreed that the British Airports Authority's EFL could be reduced by £3 million if the pay assumption was for about 7 per cent. Indeed, unless those industries negotiating early in the coming pay round were to agree relatively low settlements, it would be very difficult for industries such as British Rail to reach agreement next April to the 8 per cent which they were now assuming. It would, however, be a mistake to make unrealistic pay assumptions. It might appear to balance the books in the short term, but in practice the EFLs would quickly be shown to be inadequate.

d. The provisional assumption for the British Steel Corporation (BSC) was an EFL of £670 million. This was a very high provision for an industry which was already being heavily subsidised to the disadvantage of efficient private sector producers with which it was in competition. The possibility of reducing the assumed level of the EFL should be considered. On the other hand it would be unrealistic to take firm credit for lower figures in advance of the Corporate plan which the Chairman of BSC would be presenting to Ministers at the end of the year.

THE PRIME MINISTER, summing up the discussion, said that the Committee agreed that further savings of approximately £300 million at 1980 survey prices should be found by across the board cuts equivalent to 6 per cent of the proposed level of fixed investment by the nationalised industries, but not necessarily found by cutting investment and preferably found by limiting pay increases, improving efficiency and other methods of reducing current expenditure. This decision, which was subject to the approval of the Cabinet, recognised the difficulties

of finding the full £457 million proposed by the Chief Secretary, Treasury. It was possible that some further saving, which would contribute something towards off-setting the balance of about £150 million, would come from a reduction on the provisional EFL of £670 million for BSC, although no firm view could be reached on this until the Committee had considered the Corporation's Corporate plan at the turn of the year. It was open to sponsor Ministers to vary the severity of the percentage cuts between their industries if they wished, provided that they achieved in agregate the equivalent of a 6 per cent cut on fixed investment for all the industries for which they were responsible. They should strongly urge their industries to find the savings so far as possible by savings in current costs, from greater efficiency and low pay settlements, and from further privatisation and disposals. They should make clear to the industries that they would not accept proposals for further increases in tariffs, and particularly those applying to industrial customers, in order to meet the extra savings now being sought. Sponsor Ministers should report the outcome of their further consideration of the EFLs of the industries for which they were responsible to the Chief Secretary, Treasury, and discuss with him any difficulties in implementing the decisions. They should do so urgently with a view to agreeing the EFLs to be announced for each industry later in November.

The Committee -

1. Agreed, subject to the final approval of Cabinet, that there should be across the board cuts in nationalised industry External Financing Limits equivalent to 6 per cent of the proposed levels of fixed investment in the Investment and Financing Review attached to the Chief Secretary, Treasury's memorandum E(80) 64.

2. Invited sponsor Ministers -

i. to be guided by the Prime Minister's summing up of their discussion in advising the nationalised industries on the form of these further savings.

ii. in the light of their further discussions with the industries, to agree urgently with the Chief Secretary, Treasury, the External Financing Limit in 1981-82 for each nationalised industry.

5. INDUSTRIAL ENERGY PRICING

The Committee had before them memoranda by the Secretary of State for Energy (E(80) 120 and 128) about industrial energy prices.

THE PRIME MINISTER said that the Committee would discuss these memoranda at a later meeting. In the meantime they agreed that the Secretary of State for Energy should be free to make a public statement based on the six points summarised in paragraph 12 of his memorandum E(80) 128.

The Committee -

1. Agreed to discuss at a later meeting the memoranda E(80) 120 and 128.

2. Agreed, that in the meantime, the Secretary of State for Energy should make a public statement, if he wished, based on the proposals summarised in paragraph 12 of his memorandum (E(80) 128).

Cabinet Office

7 November 1980