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Ref. A01403

PRIME MINISTER

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Equity Investment Scheme - Tax Reliefs for Small Firms

(E(80) 11)

BACKGROUND

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The Committee last considered this on 12th December (E(79) 17th Meeting, Item 2) when there were two options available, both designed 'to encourage enterprise and the growth of the small firms sector'. Two main schemes were:

- (a) The 'losses' scheme, now retitled the 'risk sharing' scheme;
- (b) the 'start-up' scheme.

2. There was a strong feeling in the Committee that the Chancellor should be more adventurous in the Budget, but in your summing up you left it that "the Committee could only give the Chancellor a broad indication of its views, and leave him to make the best judgment in the light of available resources nearer the time of the Budget. The Committee did not want to rule out the package of small measures to help small businesses, but it considered that, within the limits of available resources, there was much to be said for larger and more attractive schemes. Despite the difficulties, the Committee saw more attraction in the equity investment or 'start-up' scheme than in the so-called 'losses' scheme ....".

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3. Since then, the Chancellor has reconsidered the proposal; but his letter of 21st January to the Secretary of State for Industry comes down firmly against any kind of 'start-up' scheme. (The paper attached to that letter is the best available account of the schemes themselves). This drew strong reactions from the Secretaries of State for Industry and for the Environment, and you asked (29th January) that the subject should go to E. The Chancellor demurred: and tried to persuade the two Secretaries of State to fall in line with his preference for the 'losses' scheme. They refused, returned to the charge, and you again ✓ ruled (Mr. Lankester's letter of 8th February) that the subject should go to E,

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on the basis of a 'collective brief' from the CPRS. Even that did not dispose of the matter, because Mr. Heseltine has returned to the charge (minute dated 12th February) pressing the argument for a 'start-up' scheme, in almost exactly the form described in the Chancellor's note of 21st January. (The original start-up scheme actually began life in the Department of Industry).

4. The essential issue before the Committee comes out clearly from the CPRS paper. Is the package proposed by the Chancellor, including the 'losses' or 'risk sharing' scheme, good enough; or should the 'start-up' scheme be added to it?

5. The argument for the 'start-up' scheme is that it is much more positive and exciting than the rest of the package and will do more to encourage genuine new investment (not just expansion of existing small business). The argument against is the scope for abuse, the cost, and the poor return compared with other Budget options. To reduce the abuse means fencing the scheme round so much that the Chancellor does not think it worth the effort, still less the cost. Mr. Heseltine believes the Chancellor, and the CPRS paper, do insufficient justice to the merits of the start-up scheme, and believes that the Inland Revenue have over-emphasised the objections. Inland Revenue for their part do not think that Mr. Heseltine's minor modifications (advance certification by an accountant, etc.) make any practical difference.

HANDLING

6. I suggest you start by asking Sir Kenneth Berrill to introduce his 'background brief', and then ask the Committee whether they are satisfied with the rest of the Chancellor's package. If they are, the question comes down to a choice between the 'risk sharing' scheme, the 'start-up' scheme or a combination of the two. You might invite the Secretary of State for Industry to make the case for the start-up scheme; ask the Chancellor to rehearse the arguments against it; and then call the Secretary of State for the Environment to rebut some of the Inland Revenue arguments. Thereafter you can throw open the discussion more generally.

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7. Tactics will be difficult. There is clearly a strong feeling among certain Ministers that the Chancellor is being too cautious. Equally, you will not wish to be seen to overrule the Chancellor on a Budgetary matter. I would imagine you will want to end up, as last time, with a 'take note' conclusion, inviting the Chancellor to do the best he can in the light of points made in this discussion, but noting the substantial difficulties in the way of a start-up scheme. You may also wish to add (as a genuine contribution, not just a consolation prize) the thought, in paragraph 11 of the CPRS paper, that there should be a study made of the start-up scheme, involving the use of outside tax consultants or tax counsel. Inland Revenue have suggested to us that the real need is not so much tax lawyers, but consultation with City interests: perhaps this could also be provided for.

CONCLUSIONS

8. The conclusions might be on the lines set out in the preceding paragraph.

REA

(Robert Armstrong)

12th February, 1980