
Budget 2002

The strength to make long-term decisions: Investing in an enterprising, fairer Britain

**Economic and Fiscal Strategy Report and
Financial Statement and Budget Report
April 2002**

Return to an Order of the House of Commons dated 17 April 2002

*Copy of Economic and Fiscal Strategy Report and Financial Statement and Budget Report – April 2002
as laid before the House of Commons by the Chancellor of the Exchequer when opening the Budget.*

Paul Boateng
Her Majesty's Treasury
17 April 2002

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The Economic and Fiscal Strategy Report and the Financial Statement and Budget Report contain the Government's assessment of the medium-term economic and budgetary position. They set out the Government's tax and spending plans, including those for public investment, in the context of its overall approach to social, economic and environmental objectives. After approval for the purposes of Section 5 of the European Communities (Amendment) Act 1993, these reports will form the basis of submissions to the European Commission under Article 99 (ex Article 103) and Article 104 (ex Article 104c) of the Treaty establishing the European Union.

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OVERVIEW

Budget 2002, *The strength to make long-term decisions: Investing in an enterprising, fairer Britain*, comprises the Economic and Fiscal Strategy Report (EFSR) and the Financial Statement and Budget Report (FSBR).

The EFSR sets out:

- **the Government's long-term goals and the comprehensive strategy it is pursuing to achieve them;**
- **the progress that has been made so far; and**
- **the further steps the Government is taking in Budget 2002 to advance its long-term goals.**

The FSBR provides:

- **a summary of each of the main Budget measures and how they affect the Budget arithmetic; and**
- **updated assessments and forecasts of the economy and the public finances.**

INTRODUCTION

1.1 The Government's objective is to build a stronger, more enterprising economy and a fairer society, extending economic opportunity and supporting those most in need to ensure that rising national prosperity is shared by all.

1.2 Stability, productivity and employment opportunity are the foundations of the Government's economic strategy. Over the past five years, the Government has taken tough decisions and introduced wide-ranging reforms to deliver high and stable levels of growth and employment, establishing a platform of economic stability based on low inflation and sound public finances. Rising national prosperity has allowed the Government to devote more resources to its priorities – including reducing poverty among children and pensioners and investing more in reform of Britain's public services.

1.3 Last year, global economic conditions posed significant challenges for policy-makers. Weaker growth, falling business confidence and increased uncertainty in the aftermath of 11 September tested the economic strength of countries around the world. Because the UK entered this period with sound economic fundamentals and a policy framework that was well placed to respond to the risks, the economy proved better able to cope with global instability than on previous occasions, growing faster than any other G7 economy over the year as a whole.

1.4 Just as the Government took tough decisions on the economy to deliver economic stability, it must now have the strength to take the long-term decisions necessary to build a stronger, fairer, and more enterprising Britain. Budget 2002 introduces further important reforms to promote work and enterprise, tackle poverty and deliver the sustained investment needed to modernise Britain's public services, raising standards to the level of the best. The Budget advances the Government's long-term goals of:

- maintaining economic stability, ensuring that the fiscal rules are met, inflation remains low, and the UK has faster productivity growth than its main competitors;

- sustaining a higher proportion of people in employment than ever before, while seeking to ensure full employment in every UK region;
- eradicating child poverty and tackling pensioner poverty, extending opportunity for all children and providing security for all pensioners;
- establishing world-class public services, delivering investment to improve national healthcare for all, raise standards in education, modernise Britain's transport and tackle crime; and
- tackling global poverty and climate change, helping to achieve the international community's Millennium Development Goals by 2015, and achieving the UK's commitments under the Kyoto Protocol.

MAINTAINING MACROECONOMIC STABILITY

I.5 The Government's goal is to maintain long-term economic stability, with low and stable inflation and sound public finances. Chapter 2 describes how the Government is working to achieve its goal and summarises prospects for the UK economy and the public finances, full details of which are set out in Chapters B and C of the FSR.

The policy framework

I.6 The Government's macroeconomic policy framework is based on the principles of transparency, responsibility and accountability, and is designed to ensure lasting economic stability to allow businesses, individuals and the Government to plan effectively for the long-term. The Bank of England has operational independence to set interest rates to meet the Government's inflation target, while fiscal policy is underpinned by two strict fiscal rules which ensure sound public finances over the medium-term. The fiscal rules underpin the Government's public spending framework which reinforces incentives for long-term planning and delivers a sharper focus on the quality and outcome of public service provision. These policies work together in a coherent and integrated way.

I.7 Since the new policy frameworks were introduced, the economy has experienced a period of stability and growth. Employment has risen to record levels and inflation has been lower and more stable than in the past. Tough decisions on taxation and spending taken over the course of the last Parliament have put the public finances on a sustainable footing, freeing up resources for investment in public services and allowing fiscal policy to support monetary policy during last year's slowdown in the global economy.

The economy

I.8 GDP in the major G7 economies grew by just 1 per cent last year, in line with the Pre-Budget Report forecast. For the first time since 1974, growth slowed significantly and simultaneously in the US, Europe and Japan, accompanied by sharp declines in world trade growth, investment, industrial production and stock markets. Prospects for G7 growth this year have however improved since the time of the Pre-Budget Report and the US economy is now expected to propel a G7 recovery during 2002. In the Budget 2002 forecast:

- **G7 GDP** is expected to grow by 1½ per cent in 2002, rising to 2¾ per cent in 2003; and
- **world trade** is expected to grow by 2¼ per cent in 2002, before picking up in 2003 as the global recovery gathers pace. UK export markets are expected to mirror this trend, rising by just 1¾ per cent in 2002 before growth picks up to almost 8 per cent in 2003.

I.9 In the UK last year, sound economic fundamentals and decisive macroeconomic policy action supported domestic demand and ensured that the economy coped well with the global economic slowdown and rising uncertainty. The economy grew by 2.2 per cent in 2001, in line with the Pre-Budget Report projection and the lower end of the Budget 2001 forecast

range. Growth is expected to strengthen and become more balanced over the forecast period as stronger external demand provides impetus to investment and exports. In the Budget 2002 forecast:

- **GDP** is expected to increase by 2 to 2½ per cent in 2002, rising to 3 to 3½ per cent in 2003 before returning to trend in 2004;
- the economy is continuing to experience its longest period of sustained low inflation since the 1960s. **RPIX inflation** is expected to remain close to the Government's 2½ per cent target over the forecast period; and
- while the downside **risks** associated with the terrorist attacks of 11 September have diminished since the Pre-Budget Report, prospects for UK growth will continue to be affected by the pace and timing of the global recovery. However, with sound public finances and low inflation, policy is well placed to respond to continuing risks.

Trend growth **I.10** The economic projections presented in this Budget are anchored on a neutral assumption of 2¾ per cent for annual trend output growth over the period. This revised estimate underpins the mid-points of the Budget 2002 economic forecast ranges and is in line with those produced by a number of independent organisations, including the IMF. The revision partly reflects the impact of higher assumed growth in the working age population due to migration. Maintaining previous practice, no allowance has been made for productivity improvements associated with the Government's strategy for raising the UK's productivity performance. For reasons of prudence, the projections of the public finances presented in this Budget are based on an assumption for trend output growth that is ¼ percentage point lower than the Government's neutral view. The National Audit Office have judged that using a 2½ per cent trend growth rate as the basis for the fiscal projections is reasonable and cautious.

The public finances **I.11** The slowdown in the world economy affected the fiscal balances last year. The provisional outturn for the current budget in 2001-02 shows a surplus of £10.6 billion, compared with a projection of £16 billion at the time of Budget 2001. The provisional outturn for net borrowing in 2001-02 is £1.3 billion, compared with a projected net repayment of £5 billion in Budget 2001. The provisional outturn estimates are close to those identified in the Pre-Budget Report interim forecast.

I.12 The change over the past year has been driven largely by a reduction in receipts – particularly of corporation tax – caused by weaker global growth, lower equity prices and a deterioration in financial companies' profits. Lower receipts have been only partly offset by further non-discretionary savings in Annually Managed Expenditure (AME) as the benefits of lower unemployment and sound public finances have led to lower social security and debt interest payments.

Budget decisions **I.13** Against this backdrop, the Government is now taking further long-term decisions to advance its goals. Budget 2002:

- **introduces a package of measures to encourage enterprise**, supporting business growth and development by rewarding innovation and reducing regulation and compliance costs;
- **takes further steps to promote employment**, improving work incentives for people on low incomes, and targeting further assistance on those groups and regions facing the most serious barriers to work;
- **introduces new measures to tackle child poverty**, supporting families with

children in recognition of the costs and responsibilities that come with parenthood;

- **takes action to protect the government revenue base and close loopholes in the tax system**, tackling tax fraud and avoidance, and promoting fairness;
- **adds £4 billion to Departmental Expenditure Limits** in 2003-04 and **sets firm overall spending limits** for the three-year period of the 2002 Spending Review, allowing:
 - **current spending**, excluding spending on health, to increase by 2½ per cent a year in real terms in 2004-05 and 2005-06. Current spending will rise in total by an average of 3.3 per cent a year in real terms over the same period; and
 - **public sector net investment** to rise from its 1.8 per cent of GDP target in 2003-04 to 2 per cent of GDP by 2005-06, continuing to address the legacy of under-investment in Britain's public infrastructure, while meeting the sustainable investment rule.
- within the overall envelope for public spending, and in response to the recommendations of the Wanless Review of long-term health trends, delivers substantial increases in investment to place the National Health Service (NHS) on a sustainable long-term financial footing and ensure that resources are available for reform. The Budget provides for **7.4 per cent average annual real terms growth in UK NHS spending over the five years to 2007-08, and 7.5 per cent growth in England**.

I.14 After allowing for non-discretionary changes to receipts and spending, and taking into account the Budget decisions – including significant increases in resources for the National Health Service – the Government remains on track to meet its strict fiscal rules. In order to ensure sound public finances over the medium-term:

- from April 2003, there will be an **additional one per cent national insurance contribution (NIC) by employers, employees and the self-employed on all earnings above the NICs threshold**. This is in addition to existing rates of contribution below the upper earnings limit for employees and the upper profits limit for the self-employed. These limits will be increased in line with inflation in 2003-04; and
- **the income tax personal allowance for those aged under 65 and the NICs threshold will be frozen** in 2003-04.

Meeting the fiscal rules

I.15 The surplus on the current budget is expected to decline from 1.1 per cent of GDP in 2001-02 to 0.3 per cent of GDP in 2002-03. Thereafter, it is expected to rise to 0.7 per cent in 2006-07. On a cyclically-adjusted basis, the current budget is expected to remain in surplus throughout the forecast period, while the average surplus since the start of the current cycle also stays positive throughout, leaving the Government on track to meet the golden rule, including in the cautious case. Public sector net debt is expected to remain low and stable at around 31 per cent of GDP – comfortably meeting the sustainable investment rule, and well below 40 per cent.

Table I.1: Fiscal balances compared with Budget 2001 and the 2001 Pre-Budget Report¹

	Outturn ²			Projections			
	2000–01	2001–02	2002–03	2003–04	2004–05	2005–06	2006–07
Surplus on current budget (£ billion)							
Budget 2001	22.3	15.9	14	8	9	9	–
PBR 2001	25.1	10.3	3	4	7	8	9
Budget 2002	21.6	10.6	3	7	9	7	9
Net borrowing (£ billion)							
Budget 2001	–15.0	–4.7	2	10	11	12	–
PBR 2001	–18.8	2.5	12	15	13	13	13
Budget 2002	–15.9	1.3	11	13	13	17	18
Cyclically-adjusted surplus on current budget (per cent of GDP)							
Budget 2001	2.0	1.2	1.0	0.6	0.7	0.7	–
PBR 2001	2.3	1.0	0.3	0.3	0.5	0.7	0.7
Budget 2002³	1.8	1.0	0.5	0.6	0.7	0.6	0.7
Cyclically-adjusted net borrowing (per cent of GDP)							
Budget 2001	–1.3	–0.1	0.4	1.1	1.1	1.1	–
PBR 2001	–1.6	0.3	1.1	1.4	1.2	1.1	1.1
Budget 2002³	–1.2	0.2	0.9	1.2	1.2	1.4	1.4
Public sector net debt (per cent of GDP)							
Budget 2001	31.8	30.3	29.6	29.7	29.9	30.0	–
PBR 2001	31.2	30.7	30.6	31.0	31.1	31.1	31.1
Budget 2002³	31.3	30.4	30.2	30.4	30.4	30.7	31.0

¹ Excluding Windfall Tax receipts and associated spending.

² The 2000–2001 figures were estimates in Budget 2001. The 2001–02 figures were projections in Budget 2001 and PBR 2001.

³ These figures are estimates in 2001–02.

I.16 The Budget also locks in the fiscal stance in the Pre-Budget Report this year and over the next two years. Compared with the Pre-Budget Report, there is a small fiscal tightening this year and next as growth gathers pace and the economy returns to trend.

I.17 Consistent with the requirements of the *Code for Fiscal Stability*, Annex A of the EFSR presents illustrative long-term fiscal projections and examines the long-term sustainability of the public finances. The projections indicate that the UK has a broadly sustainable fiscal position in the long term and that the impact of an ageing population on the public finances is expected to be both manageable, and less marked than in most other EU countries.

MEETING THE PRODUCTIVITY CHALLENGE

I.18 Raising the UK's sustainable rate of productivity growth is central to the Government's economic strategy. Improving Britain's productivity performance is a key route to higher prosperity and living standards and advances the Government's objectives to tackle poverty and improve public services. Chapter 3 describes the steps the Government is taking to achieve its long-term goal of ensuring that the UK achieves faster productivity growth than its main competitors, closing the productivity gap which exists between the UK and many other advanced industrial economies.

Measures so far I.19 The Government has taken significant steps to raise Britain's productivity growth, focusing its action on five important drivers of productivity performance:

- **competition:** through strengthened powers for the Office of Fair Trading and improvements to the overall competition regime introduced in the

Competition Act 1998, as well as detailed investigations into competition in specific markets, including banking and the professions;

- **enterprise and innovation:** through reduced corporation tax rates and important reforms to capital gains tax, a Share Incentive Plan and improvements to Enterprise Management Incentives to help smaller companies recruit and retain highly-skilled people, a research and development (R&D) tax credit for small and medium-sized companies, and an exemption from stamp duty for property transfers up to £150,000 in Britain's most disadvantaged areas;
- **investment:** with a comprehensive review of institutional investment in the UK, proposals to improve dramatically the flexibility, speed and responsiveness of the land-use planning system; and public spending plans that reverse the legacy of under-funding of Britain's public infrastructure;
- **skills:** by providing substantial extra resources to raise standards in primary and secondary schools and additional funding for higher education places; and
- **public sector productivity:** with a greater focus on outcomes for public service delivery through Public Service Agreements (PSAs), Departmental Investment Strategies (DISs) to improve public sector investment, and the creation of an Office for Government Commerce to deliver more efficient procurement across government.

Budget measures 1.20 The Government's Enterprise Bill will enhance the UK's competition regime and modernise the laws on insolvency, bringing down the barriers to enterprise and entrepreneurial activity. Budget 2002 introduces further measures to support enterprise and the drivers of productivity growth, including:

- a reduction in the **corporation tax starting rate from 10 per cent to zero** from April 2002, meaning that 150,000 companies will no longer pay any corporation tax;
- a reduction in the **small companies' rate of corporation tax by 1 percentage point to 19 per cent** from April 2002, benefiting a further 335,000 companies;
- a package of measures to **reduce the burden of VAT and payroll administration** to simplify the tax system and reduce compliance costs for small businesses;
- reforms to establish a **modern and competitive business tax system**, including an exemption for gains and losses on substantial shareholdings; relief for the costs of intellectual property, goodwill and other intangible assets; and a new regime for the taxation of loan relationships, derivative contracts and foreign exchange gains and losses;
- **abolishing stamp duty** for non-residential property transfers in disadvantaged areas and a new **Community Investment Tax Credit** to promote enterprise and wealth creation in under-invested communities;
- a new **volume-based research and development tax credit for large companies** to boost the UK's innovation performance;
- **Employer Training Pilots to test new measures to improve access to training** and enable employees to attain basic and level 2 skills; and
- additional funding of **£30 million to help small organisations attain Investors in People** status.

INCREASING EMPLOYMENT OPPORTUNITY FOR ALL

I.21 The Government's long-term goal is to sustain a higher proportion of people in work than ever before by the end of the decade. The strength of the economy depends on the number of people in work and how productive they are. For the majority of individuals and their families, employment is also the single most effective means of avoiding poverty, both now and in the future. Chapter 4 describes the steps the Government is taking to advance its goal, ensuring that employment opportunity is extended to all groups and every area in the country.

Measures so far I.22 The Government's strategy for delivering higher than ever levels of employment focuses on helping people move from welfare to work, targeting extra support on those areas and groups that face the most serious barriers to work, and making work pay. It has introduced a wide range of measures in each of these areas:

- **welfare to work:** reducing structural unemployment through the New Deal programmes for young people and the long-term unemployed, addressing concentrations of economic inactivity through the New Deal programmes for lone parents and people with disabilities, and launching Jobcentre Plus to provide an active, employment-focussed service to all working age benefit recipients;
- **tackling regional worklessness:** establishing Action Teams to tackle deep-seated employment problems in disadvantaged areas, and creating a new Rapid Response Service to support people affected by large-scale redundancies, especially in deprived areas; and
- **making work pay:** with reforms to the tax and benefit system underpinned by the National Minimum Wage, the introduction of the Working Families' Tax Credit (WFTC) and the Disabled Person's Tax Credit (DPTC) to improve work incentives among families with children and people with disabilities, simplified extended payments in Housing Benefit, and increased childcare provision and support through the National Childcare Strategy.

Budget measures I.23 Budget 2002 takes further steps to promote work, ensuring that every person in every area of Britain who is able to work has the opportunity to do so:

- the **basic credit in the Working Families' and Disabled Person's Tax Credits** will be increased by £2.50 a week from June 2002, on top of the increases in line with indexation in April 2002;
- the new **Working Tax Credit** will be introduced from April 2003 to help tackle poor work incentives and persistent poverty among working people, including those without children. On its introduction, the Working Tax Credit will guarantee minimum incomes of:
 - £183 a week for a single earner couple without children, aged 25 or over and working full time on the minimum wage; and
 - £237 a week for a family with one child and one earner working full time on the minimum wage.
- **the New Deal 25+ will be extended** in pilot areas to jobseekers who have been unemployed for a total of 18 months over the previous three years. Pilots will identify eligible individuals at their six month Restart interview;
- **mandatory Gateway to work courses** will be introduced for all jobseekers on the New Deal 25+ in London, Manchester, Dundee and Swansea;

- a new **mentor service** will start to be introduced to provide advice and support to lone parents seeking to enter work;
- **mandatory personal adviser meetings will be extended** to all lone parents on Income Support with children under the age of five;
- **childcare coordinators** will be established in every Jobcentre plus district to improve access to information on local childcare provision;
- **eligibility for the childcare tax credit** element of the Working Tax Credit will be extended to those who use approved childcare in their own homes; and
- new funding will be made available to help **Action Teams support transport solutions** in deprived areas where travel is a barrier to work.

BUILDING A FAIRER SOCIETY

1.24 A strong and productive economy must be underpinned by fairness and social inclusion so that everyone has the chance to fulfil their potential and share in rising national prosperity. The Government has placed welfare reform at the heart of its strategy for promoting fairness, offering extra help to those who need it most – families with children, pensioners and people with disabilities. It is determined to achieve its long-term goals of abolishing child poverty and tackling pensioner poverty and is pursuing a wider strategy to reward saving, strengthen local communities, tackle global poverty and establish a modern tax system in which everyone – individuals and businesses – pays a fair share.

Measures so far 1.25 As described in Chapter 5, the Government has introduced a number of important reforms to address these priorities:

- **support for families and children:** tackling child poverty through the introduction of the WFTC and the Children's Tax Credit; targeted support for low-income parents through the Sure Start Maternity Grant; a Children's Fund to improve the support available to children, young people and their families; and increased financial support through the tax and benefit system in recognition of the costs and responsibilities that come with parenthood;
- **fairness for pensioners:** by introducing a comprehensive package of support to improve pensioners' living standards, including the Minimum Income Guarantee (MIG) uprated by earnings for the poorest pensioners, guaranteed increases in the basic state pension and a commitment to raise the basic state pension each year from 2004-05 by 2½ per cent or the increase in the September Retail Price Index if that is higher, a new Pension Credit from 2003 to ensure that low and modest income pensioners are rewarded for their savings, free TV licences for those aged 75 or over, and an annual winter fuel payment – set at £200 a year for the remainder of this Parliament – for households containing someone aged 60 or over; and
- **supporting saving:** by introducing the State Second Pension and stakeholder pensions to help people provide for security in old age, establishing Individual Savings Accounts (ISAs) and retaining the £7,000 annual contribution limit until April 2006, and consulting on the Saving Gateway and Child Trust Fund.

Budget measures 1.26 Building on this comprehensive programme of reform, the Government is taking further steps to tackle child and pensioner poverty, encourage saving, tackle global poverty and promote a modern and fair tax system.

Tackling child and pensioner poverty

I.27 To provide support for families and children and to help tackle child poverty, the Government is now:

- increasing the **child allowances in Income Support and Jobseeker's Allowance** by £3.50 a week from October 2002, in addition to the increases in the WFTC and DPTC described above;
- introducing a new **Child Tax Credit** from April 2003 to provide a single, seamless system of income-related support for families with children. On its introduction, the Child Tax Credit, and universal Child Benefit, will guarantee support of:
 - £26.50 a week for the first child for the 85 per cent of families with an income of less than £50,000 a year; and
 - £54.25 a week for the first child in families with an income of less than £13,000 a year.
- increasing the **income tax personal allowance for 65 to 74 year olds** in 2003-04 to £6,610, ensuring that no pensioner aged 65 or over will pay tax on income of less than £127 a week; and
- implementing the comprehensive package of **support for pensioners** previously announced and summarised above, including the Pension Credit from 2003 and guaranteed increases in the basic state pension.

Supporting saving

I.28 To extend the benefits of saving and asset ownership, Budget 2002 announces:

- **steps to modernise the annuities market**, to increase the choice for consumers and help to ensure that annuities provide a secure income in retirement; and
- the **launch of Saving Gateway pilot projects** in four pilot areas from August 2002.

Tackling global poverty

I.29 To promote further progress towards the international community's Millennium Development Goals, Budget 2002 introduces:

- a new **tax credit to encourage R&D into drugs and vaccines** to treat specific diseases threatening lives in the least developed countries; and
- a new **relief to encourage industry to donate medical equipment and supplies** to developing countries.

Establishing a modern and fair tax system

I.30 Budget 2002 introduces further measures to promote a modern and fair tax system, including:

- **reforms to close loopholes in stamp duty on property**, modernising the current regime and ensuring it applies fairly to all relevant transactions;
- important changes to the **North Sea tax regime** to establish a regime that raises a fair share of revenue while promoting long-term investment;

- reform of the **taxation of foreign companies' branches** operating in the UK to bring the UK into line with international practice;
- **freezing the duties on spirits, wine and beer**; introducing reduced rates of duty on beer produced by the UK's small brewing industry; increasing the duty on spirits-based coolers to the level of that on spirits; and **increasing tobacco duties** in line with inflation;
- further support through the tax system for **community amateur sports clubs and charities**, and to encourage charitable donations; and
- new **measures to tackle indirect tax fraud and unfair tax avoidance** to protect the revenue base and promote fairness.

DELIVERING HIGH QUALITY PUBLIC SERVICES

I.31 The Government's long-term goal is to deliver world class public services through sustained increases in investment and modernisation to improve performance. Strong and dependable public services are a vital part of the Government's strategy for extending opportunity, tackling poverty and social exclusion and delivering higher living standards for all. They also lay the foundations for a successful, high productivity economy. Enterprise, employment and economic stability provide the platform from which the Government is working to deliver lasting improvements in Britain's public services.

Measures so far I.32 Chapter 6 describes the steps the Government has already taken to strengthen public services, including:

- **establishing a new framework for controlling public spending** that provides greater certainty for long-term planning and ensures that resources are allocated to priority public services and linked clearly to improvements in public service delivery;
- **allocating substantial increases in resources** over the three year period of the 2000 Spending Review. As a result of economic stability, and significant savings on debt interest and social security payments, the 2000 Spending Review was able to plan an additional £50 billion of departmental spending on public services by 2003-04 compared with 2000-01;
- **strengthening the delivery of local public services** by establishing stretching new outcome-based targets with local authorities in return for greater freedoms, flexibilities and financial rewards if they succeed; and
- commissioning an independent review, led by Derek Wanless, of the **trends affecting the UK health service over the next two decades** and their implications for funding and other resource requirements. The interim report of the review was published in November 2001.

Budget measures I.33 The Government is currently conducting a Spending Review to determine how departments' programmes can most effectively deliver investment and modernisation in priority public services and to establish new departmental annual spending plans up to and including 2005-06. In Budget 2002, the Government is:

- **adding £4 billion to Departmental Expenditure Limits** in 2003-04 and **setting firm overall spending limits** for the period of the 2002 Spending Review, as described earlier in this chapter;

- publishing **Derek Wanless' final report to the Chancellor on long-term health trends**. The report identifies the main factors that will affect the health service over the next two decades and the resources required to ensure that the NHS can provide a publicly-funded, comprehensive, high quality service on the basis of clinical need;
- responding to the conclusions of the Wanless Review by immediately **allocating £2.4 billion of the new DEL addition to UK health spending**, and providing for an average annual **7.4 per cent real terms increase in UK NHS spending up to 2007-08, and 7.5 per cent in England**;
- immediately **allocating £0.4 billion of the new DEL addition to personal social services spending**, and providing for an average annual **6 per cent real terms increase in spending on personal social services over the three years to 2005-06**; and
- making these new resources conditional on a **comprehensive programme of health service reform** to ensure delivery of the Government's priorities for health and personal social services and value for money for the taxpayer. The details will be set out by the Secretary of State for Health.

PROTECTING THE ENVIRONMENT

I.34 The aim of sustainable development is to ensure a better quality of life for everyone, today and for future generations. It can be achieved by balancing economic and social progress with action to protect and improve the environment. Climate change, poor air quality and environmental degradation in urban and rural areas all threaten the quality of life for every citizen. The Government is therefore using a range of economic instruments to tackle local environmental problems and to ensure that the UK fulfils its international commitments under the Kyoto Protocol.

Measures so far I.35 Chapter 7 describes the steps the Government has already taken to deliver its environmental objectives:

- **tackling climate change and improving air quality:** through the introduction of the climate change levy in April 2001 which is encouraging business to become more energy-efficient, a range of tax incentives and reforms to promote the development and take-up of greener fuels and cleaner vehicles, and the launch of the world's first economy-wide greenhouse gas emissions trading scheme in April 2002;
- **regenerating Britain's towns and cities:** with a significant package of fiscal measures to support sustainable regeneration of urban areas, including targeted VAT reliefs, tax incentives for cleaning up contaminated land and a stamp duty exemption to promote investment and economic regeneration in deprived areas; and
- **protecting Britain's countryside and natural resources:** with continued annual increases in the standard rate of landfill tax, a new aggregates levy to tackle the environmental costs of quarrying, and continuing work to limit the harmful environmental consequences of pesticide use.

Budget measures I.36 To make further progress towards achieving its environmental objectives, while responding to the recent high and volatile levels of world oil prices, the Government is now:

- introducing **two new exemptions from the climate change levy (CCL)** for sources of electricity generation with environmental benefits, and freezing the rates of the CCL;

- introducing further **enhanced capital allowances for investments** in environmentally-friendly technologies to promote business energy-efficiency;
- freezing **the duty on the main road fuels and on road fuel gases**;
- planning to introduce **duty incentives favouring sulphur-free fuels** in 2003 and to exempt **hydrogen** from fuel duty in the future;
- **freezing vehicle excise duty (VED) rates**, introducing a new **low-carbon VED rate for cars** with the lowest emissions, and reforming **VED for motorcycles and vans** to reflect environmental benefits;
- introducing **enhanced capital allowances for business cars with low emissions** and, on a revenue neutral basis, **restructuring the fuel scale charge** from 2003-04 to relate it to carbon dioxide emissions rather than engine size;
- introducing **a distance-based lorry road-user charge** in 2005 or 2006 to ensure that lorry operators contribute to the cost of using UK roads irrespective of their nationality;
- **freezing air passenger duty** and extending the scope of the lower rates that currently apply to European Economic Area countries; and
- announcing plans to **review the use of economic instruments to deal with environmental issues associated with agriculture**.

I.37 Table 7.1 of the EFSR shows how the Government's policies fit into the overall framework of its environmental strategy. Table 7.2 sets out the environmental impact of measures which have a significant effect on the environment or which serve an environmental purpose.

BUDGET MEASURES AND THEIR IMPACT ON HOUSEHOLDS

I.38 The measures introduced in this and previous Budgets support the Government's objectives of promoting work and tackling child and pensioner poverty, while laying the foundations for further sustained investment in Britain's public services.

I.39 As a result of the freezing of the personal allowance and the one per cent rise in national insurance contributions, in 2003–04:

- a person on median earnings of £21,400 will pay an additional £3.70 a week;
- a person on 50 per cent of median earnings of £10,700 will pay an additional £1.65 a week; and
- a person on 150 per cent of median earnings of £32,100 will pay an additional £5.75 a week.

I.40 This Budget rewards work and supports families. As a result of all personal tax and benefit measures:

- a single earner family on median earnings of £21,400 and with two children will be £3.90 a week better off as a result of the Child Tax Credit;
- 50 per cent of families with children will be better off, even after the freezing of the personal allowance and the one per cent rise in national insurance contributions; and
- a single person, aged 25 or over, and working 35 hours a week at the National Minimum Wage will be £21.55 a week better off as a result of the Working Tax Credit.

I.41 As a result of the personal tax and benefit measures introduced since 1997, on average by October 2003^{1,2}:

- households will be £740 a year better off;
- families with children will be £1,200 a year better off; and
- pensioner households will be £1,150 a year better off.

I.42 As a result of personal tax and benefit reforms since 1997¹:

- by April 2003, families with children in the poorest fifth of the population will, on average, be £2,400 a year better off; and
- by October 2003², on average, the poorest third of pensioner households will be over £1,500 a year better off.

I.43 Table 1.2 lists the key Budget policy decisions and their impact on government spending and revenue. Further details are provided in Chapter A of the FSBR.

¹ Compared with an indexed 1997-98 base.

² The Pension Credit is introduced from October 2003.

Table I.2: Budget 2002 policy decisions

	(+ve is an Exchequer yield)			£ million
	2002-03 indexed	2003-04 indexed	2004-05 indexed	2002-03 non-indexed
MEETING THE FISCAL RULES AND FUNDING PUBLIC SERVICES				
1 Freeze in income tax personal allowance and national insurance thresholds	0	+700	+850	0
2 Additional class 1 primary national insurance contribution for employees	0	+3,550	+3,700	0
3 Additional class 1 secondary national insurance contribution for employers	0	+3,900	+4,100	0
4 Additional class 4 national insurance contribution for the self-employed	0	+450	+450	0
MEETING THE PRODUCTIVITY CHALLENGE				
Supporting small business				
5 Corporation tax: reduce small companies' rate to 19 per cent and starting rate to 0 per cent	-20	-265	-450	-20
6 Venture Capital Trusts – flexibility of rules	-5	-5	-5	-5
7 Revalorise thresholds for VAT registration and deregistration	0	0	0	-5
Enterprise and innovation				
8 Abolition of stamp duty on goodwill	-50	-50	-50	-50
9 Exemption for gains on substantial shareholdings	-70	-130	-150	-70
10 Capital gains tax: simplification	-10	-15	-15	-10
11 Relaxation of the rules on withholding tax for exempt bodies	-10	-45	*	-10
12 Introduction of Community Investment Tax Credit	*	-5	-5	*
13 Changes to the Construction Industry Scheme	-55	-10	*	-55
14 Reform of taxation of intellectual property	-70	-160	-190	-70
15 Research and development tax credit at 25% for larger companies	-200	-400	-400	-200
16 New rules on loan relationships, derivative contracts and foreign exchange	0	+230	+350	0
INCREASING EMPLOYMENT OPPORTUNITY FOR ALL				
17 Income tax: indexation of allowances and limits in 2002-03	0	0	0	-330
18 Working Tax Credit (WTC) for families without children	0	-250	-300	0
BUILDING A FAIRER SOCIETY				
Supporting families and communities				
19 Child Tax Credit and WTC for families with children and associated measures	-500	-2,450	-2,300	-500
20 Income tax: over-indexation of age related allowances for ages 65-74	0	-55	-75	0
21 Eligibility of home childcare for childcare tax credit	0	-10	-15	0
22 Income tax: indexation of pension schemes earnings cap	0	0	0	-5
23 Relief for community amateur sports clubs	*	-5	-10	*
24 Introduction of the Vaccines Tax Credit	*	-10	-20	*
25 Relief for gifts of real property to charities	*	-10	-20	*
26 VAT: reliefs for charity buildings	*	-10	-10	*
27 Measures to encourage charitable giving	*	-30	-20	*

Table 1.2: Budget 2002 policy decisions

	(+ve is an Exchequer yield)			£ million
	2002-03 indexed	2003-04 indexed	2004-05 indexed	2002-03 non-indexed
A modern and fair tax system				
28 Tackling stamp duty avoidance	+150	+150	+450	+150
29 Film tax relief: restriction to feature films intended for cinema release	+15	+225	+295	+15
30 Manufactured payments: restriction of tax relief	0	+15	+10	0
31 North Sea taxation: introduction of 10 per cent supplementary charge and 100 per cent first year allowances	+100	+450	+600	+100
32 Modernise taxation of foreign company UK branches	0	+350	+650	0
33 VAT anti-avoidance: face-value vouchers	0	+120	+105	0
34 VAT anti-avoidance: hire purchase agreements	+40	+45	+45	+40
35 VAT anti-avoidance: partial exemption override	+195	+185	+170	+195
36 Oils fraud strategy	+100	+290	+550	+100
Duties and other tax changes				
37 Tobacco duties: revalorisation of rates	0	0	0	+135
38 Alcohol duties: beer duty relief for small brewers	-10	-15	-15	-10
39 Alcohol duties: 2 per cent cut for cider; freeze other rates	-95	-105	-105	-5
40 Alcohol duties: increase duty on coolers to spirits rate	+170	+195	+210	+170
41 Inheritance tax: over-index threshold to £250,000	-15	-25	-30	-40
42 Mutual Assistance in Recovery of Debts: implementation of provisions	+10	+10	+10	+10
PROTECTING THE ENVIRONMENT				
43 Enhanced capital allowances for green technologies	-20	-40	-40	-20
44 Climate change levy: freeze	-15	-20	-20	0
45 Climate change levy: tax incentives for combined heat and power	-15	-15	-15	-15
Transport and the environment				
46 Extension of tax exemption for employer subsidised bus services	-10	-15	-20	-10
47 Fuel duties: freeze rates	-395	-415	-420	0
48 Air passenger duty: freeze rates	-5	-20	-20	0
49 Air passenger duty: expansion of scope of lower rate	-25	-70	-75	-25
50 VED: freeze all rates	-80	-85	-90	0
51 VED: creation of new low CO ₂ car band	*	*	-5	*
52 Reform of VED for motorbikes	-10	-10	-10	-10
53 Introduction of incentives for cleaner vans	*	*	-5	*
54 VAT simplification: annual adjustment of car fuel scale charges	0	0	0	-15
TOTAL BUDGET MEASURES	-905	+6,115	+7,640	-565

* Negligible.

ADDITIONAL BUDGET POLICY DECISIONS¹

Additions to DEL	0	-4,000
Resetting of AME margin	+180	-525

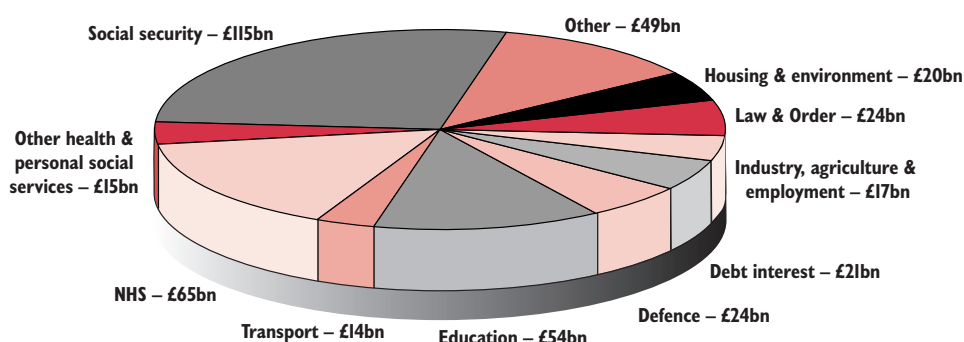
¹ See Table 2.4 for details of the envelope for the 2002 Spending Review. Final decisions on the split between DEL and AME will be taken in the Spending Review.

GOVERNMENT SPENDING AND REVENUE

I.45 Chart 1.1 presents public spending by main function. Total public spending (Total Managed Expenditure – TME) is expected to be around £418 billion in the current financial year, 2002-03. TME is divided into Departmental Expenditure Limits (DEL), shown in Table C14 of the FSBR, and Annually Managed Expenditure (AME), shown in Table C11 of the FSBR. A number of DELs, particularly those of the devolved administrations, contribute to spending on more than one function. Chart 1.1 also includes spending by local authorities, rather than the grants they receive from central government, which are included in Tables C11 and C14 of the FSBR.

Chart I.1: Government spending by function

Total managed expenditure: £418 billion

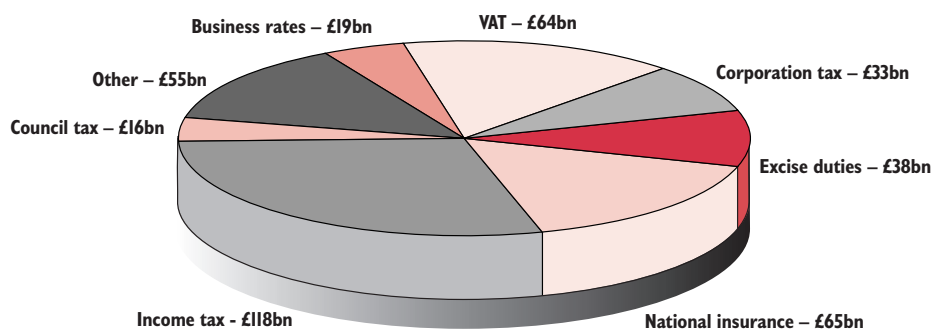


Source: HM Treasury, 2002–03 projections. Other expenditure includes spending on central administration; culture, media and sport; international cooperation and development; public service pensions; plus spending yet to be allocated and some accounting adjustments.

I.46 Chart 1.2 shows the different sources of government revenue. Public sector current receipts are expected to be around £407 in 2002-03. Table C7 of the FSBR provides a more detailed breakdown of receipts consistent with this chart.

Chart I.2: Government receipts

Total receipts: £407 billion



Source: HM Treasury, 2002–03 projections. Other receipts include capital taxes, stamp duties, vehicle excise duties and some other tax and non-tax receipts (eg. interest and dividends).