

Budget 2004

REGIONAL PRESS NOTICE

17 March 2004

PRUDENCE FOR A PURPOSE: A BRITAIN OF STABILITY AND STRENGTH: THE NORTH EAST

A series of measures that will promote greater flexibility and fairness in the North East were announced by the Chancellor today.

To ensure that national policy is designed with its impact on the North East in mind, One North East along with the other Regional Development Agencies (RDAs), were asked to contribute policy advice for Budget 2004 in 5 areas: barriers to business start-ups; provision of government services to small businesses; access to finance for small and medium-sized firms; barriers to skills provision and knowledge transfer between businesses and universities. This press notice responds in full to the RDAs' submissions.

One North East has also worked with the other RDAs to identify the top ten institutional barriers that they believe are currently hindering effective coordination of policy-decisions and service delivery in the regions. The Government believes that providing regions with the flexibility to harness indigenous strengths and tackle specific regional and local needs is key to improving the economic performance of all the regions. The Government has published today its response to the RDAs' top ten institutional flexibilities in *Devolving decision making: 2 – Meeting the regional economic challenge: Increasing regional and local flexibility*.

As a valuable contribution to the Government's commitment to achieving a greater regional balance of economic activity, Sir Michael Lyons published on Monday his final report, *Well Placed to Deliver? – Shaping the Pattern of Government Service*, which sets out a series of recommendations for relocating civil servants and other public sector workers from London and the South East.

Measures which are particularly relevant to individuals and businesses in the North East include:

- devolving regional and local Business Link services from the Department of Trade and Industry to the RDAs. This could potentially benefit 97,000 businesses in the North East;
- further details of the Local Authority Business Growth Incentives scheme. From 2005, local authorities can retain a proportion of the growth in local business rate revenues as an incentive to promote local economic growth. Over £50 million could be retained by local authorities in the North East over 3 years;
- further measures to tackle employability in enterprise areas, including the Business Premise Renovation Allowance. This will benefit the 208 most deprived wards in the North East;
- extending eligibility for the VAT cash and annual accounting schemes, which could benefit 300 eligible businesses in the North East;
- extending the Employer Training Pilot, currently running in Tyne and Wear and introducing a new pilot covering the whole of the North East;
- a New Deal for skills to ensure that individuals are helped to develop the skills they need for employment and employers can develop the skilled workforce needed for the success of their business;
- following the Skills Strategy announcement, up to 542 adults in the North East will be entitled to free training for a first level 2 NVQ;
- introducing a new definition of R&D from 1 April 2004, which will make it easier for up to 45 small and 50 large companies undertaking R&D in the North East to claim the credit, and extending the range of costs that qualify for the credit to include power, water, fuel and software costs;
- the Barker Review of housing supply, published today, concludes that house building must rise substantially to reduce house price inflation and increase the number of affordable homes. The Government agrees with the need for a significant increase in housing development over time. It intends to implement a programme of reform to planning and delivery of development as recommended in the Review and consider a package of measures to increase housing supply, including social housing investment, alongside a Planning-gain supplement by end of 2005;

- publication of a consultation document to inform the preparation of a ten-year investment framework for science and innovation as part of the 2004 Spending Review, committing to grow public investment in the science base faster than the trend rate of GDP growth over the next Spending Review period;
- piloting of mandatory work-focused interviews for some existing incapacity benefits claimants in the Pathways to Work pilot areas, alongside a job preparation premium to reward relevant activity that supports a return to work. The provision will start from January 2005 in the first wave of Pathway areas, and will extend in April 2005 to the second wave of areas, including Gateshead and South Tyneside;
- from October 2004, an increase in the adult National Minimum Wage rate to £4.85 and the youth development rate to £4.10, benefiting at least 110,000 people in the North East;
- significant reform of housing benefit from April 2004, including a £12.32 earnings disregard to strengthen work incentives for tenants;
- extra £100 help announced today with council tax and other living expenses this year for households with someone aged 70 or over. This will benefit 223,840 pensioner households in the North East;
- raising the Pension Credit guarantee element to £105.45 for single pensioners and £160.95 for couples, from April 2004. 136,270 pensioner households in the North East are eligible to benefit;
- as announced in the 2003 Pre-Budget Report, an increase in the child element of the Child Tax Credit by £180 to £1,625 a year from April 2004, equivalent to a weekly increase of £3.50. 118,500 working families in the North East are eligible to benefit;
- roll out of Education Maintenance Allowances, providing up to £1,380 for young people pursuing education, dependent on household income, benefiting up to 21,000 16 to 18 year olds in the North East in 04/05, 26,000 in 05/06 and 27,000 in 06/07;
- a minimum wage for 16-17 year olds of £3 per hour from October 2004; and
- firm spending plans for the Department for Education and Skills' departmental expenditure limit and local authority formula spending

share on education and children for 2004-05 to 2007-08. England education spending will grow by an annual average of 4.4% in real terms across the 2004 Spending Review period and by 2007-08, education spending will be £7.4 billion higher than in 05-06 and £12 billion higher than in 04-05. By 2007-08, education spending in the UK will be 5.6% of GDP, up from 5.4% in 2004-5. Since 1997, the Government has provided for 500 extra teachers and 4,500 extra support staff in the North East.

The Treasury will be publishing a leaflet setting out more detail about the Budget and explaining what it means for the North East.

ANNEX: RESPONDING TO THE RDAs' INPUT INTO BUDGET 2004

This Annex outlines the input made by the RDAs for Budget 2004, and the Government's response to each of their recommendations.

1. BUSINESS START-UPS

RDA recommendation: A review of the regulatory and tax structures affecting small businesses would be welcome to identify areas for simplification and reducing the administrative burden. We welcome the proposals announced in the 2003 Pre-Budget Report in this regard, especially the VAT changes.

Government response: The Government keeps all aspects of the tax system under review at all times, and Budget 2004 builds upon a number of existing measures that simplify the tax system for smaller businesses such as the VAT flat rate scheme and consultation on reforms to corporation tax.

The O'Donnell Review has examined the institutional framework of tax administration and policy-making at a high level. The Government aims to leverage the benefits of a more coordinated tax policy system with simplified delivery from the customer's perspective

RDA recommendation: We welcome the review of welfare benefits for new entrepreneurs and encourage the vigorous pursuit of this agenda, including

piloting the “Offer in Compromise” US model of benefits and tax amnesties for firms moving into the regulated economy.

Government response: The review of the routes from benefits to self-employment was announced in the 2003 Pre-Budget Report and is being conducted by the Small Business Service with the support and encouragement of the Treasury and Department for Work and Pensions. Small business groups have told us that the system works better for employees, rather than the self employed. We want to explore whether this is true, and what could be done. The unemployed may face particular barriers when seeking to pursue self-employment. It is important that we provide the right support and advice and encourage entrepreneurship as an option available to all.

RDA recommendation: Encourage the European Union to develop a block State Aids exemption for measures to support the development of entrepreneurship.

Government response: Modernisation of the state aids system is an important issue for the Government. We are building support throughout Europe for our belief that state aid should be targeted so as to tackle identified market failures with tighter controls on the most distortive aids. For example, the Government is seeking reforms of the most regional state aids rules to allow better targeting of aid, and has worked with the Commission on proposals for a significant impact test to allow swifter approval for small, non-distorting aids. Within the UK, the Government is implementing measures to promote entrepreneurship such as schemes to provide access to finance for new innovative high growth firms and for firms in disadvantaged areas. The RDA’s voice in this debate is a valuable one, adding weight to the Government’s position with our partners in Europe and the Commission.

RDA recommendation: Urge caution in the proposed development of NIC on SME dividend payments, any changes must not adversely affect the incentives to invest.

Government response: The Government stated in the 2003 Pre-Budget Report that it would bring forward proposals in the Budget “to ensure that the right amount of tax is paid by owner managers of small incorporated businesses on the profits extracted from their company”. The Government announces today specific proposals to ensure that the measures it has introduced provide support for businesses that reinvest their profits and grow their businesses. The Government will also take steps to reinforce compliance with the tax system by the smallest companies, while ensuring

that compliant businesses do not face additional burdens. The measures announced today are:

- a minimum corporation tax rate of 19% on profits distributed on or after 1 April 2004; and
- the requirement for newly incorporated businesses to disclose basic tax information will be strengthened.

The Government will also consider measures to strengthen anti-avoidance legislation on loans made to shareholder directors of close companies.

To ensure that targeted tax incentives support the Government's objectives for growth, enterprise and productivity, the Government proposes to consider the issues raised by the interaction with the tax system of definitions of self-employed, employed and the remuneration paid to owner-managers, in a discussion paper which will be issued at the time of the 2004 Pre-Budget Report.

2. GOVERNMENT SERVICES FOR SMALL BUSINESSES

RDA recommendation: Extend the Business Link Pilots to all regions to improve co-ordination of publicly funded business support services.

Government response: The RDAs have an important role to play in the delivery of business support. Government believes that the opportunity to deliver business support services in a more flexible, targeted and innovative way is greater if they are delivered from the regional level.

To improve the connections between Business Link Operators and the RDAs and to explore the scope for more effective business support at the regional and local level, the Government introduced a number of RDA-led business support pilots in the 2002 Spending Review. These were launched in April 2003 in the West Midlands, the East Midlands and the North West, where they are developing new approaches to coordinating the delivery of Business Link services. The aim of the pilots is to grant the RDAs the discretion to manage contracts with Business Link Operators so that they can tailor support to the key challenges of their local areas.

The pilots enable the RDAs to better integrate business support services with their wider economic strategies, enhance targeting of local barriers to enterprise and improve policy design and delivery to address these barriers.

They have generated substantial interest in non-pilot areas. As set out in *Devolving decision making: 2 – Meeting the regional economic challenge: Increasing regional and local flexibility*, the Government is announcing today that it will devolve regional and local Business Link services to the RDAs, with a framework for setting national standards and services to be developed with SBS, the RDAs and other Government departments funding business support.

RDA recommendation: Regionalise the approach and services for business support for rural and land-based business in line with the recommendations of the Haskins report.

Government response: The Haskins' Rural Delivery Review was published in November 2003. Two of its key principles are the separation of policy and delivery and the devolution of delivery. Specifically, the review recommends, for example, that RDAs should have the lead responsibility in co-ordinating public sector rural business support and advice. The Government is currently discussing these proposals with the RDAs, and expects to publish a full response over the course of the next few months.

RDA recommendation: Jointly investigate greater scope for innovative approaches to supporting the market for good quality SME advice (e.g. voucher schemes).

Government response: The RDAs and central government will continue to work closely together when developing business support services. The Government believes that there is greater flexibility and scope for innovation in business support at the regional level. That is why the Government announces today its intention to devolve regional and local Business Link services to the RDAs. This regional devolution of responsibility for Business Link services will allow the RDAs greater autonomy in developing innovative approaches to delivering business support at the regional and local level, within a national framework to be developed with SBS, the RDAs and other Government departments funding business support.

3. ACCESS TO FINANCE FOR SMALL AND MEDIUM-SIZED FIRMS

RDA recommendation: Ensure a strong regional dimension to the proposed 'pathfinder' round of Enterprise Capital Funds (funding up to £2 million per SME).

Government response: The Government intends to launch a pathfinder round of Enterprise Capital Funds (ECFs). ECFs will be commercial funds, investing a combination of private and public monies in small high-growth businesses. The aim of the funds is to encourage flow of private capital into the 'equity gap', and to lower barriers to entry for new risk capital managers. The Pathfinder round of funds will be allocated through a competitive bidding process.

The Government will encourage innovative bids for the pathfinder round, which is intended to test the scope and appetite for the scheme. Where the business plan or investment strategy would be enhanced by a specific regional focus, the Government would welcome such an application. However, there will be no specific assessment bias in favour or against regionally based bids within the competitive process.

RDA recommendation: Consider increasing the incentives for Venture Capital Trusts to provide equity funds for smaller investments (under £100,000).

Government response: The Government has considered all of the representations that it has received since making proposals in the 2003 Pre-Budget Report to bring forward enhanced incentives for individuals investing in Venture Capital Trusts (VCTs). The Budget announces that, to smooth the flow of funds into VCTs, and provide a short-term stimulus to the market it will:

- withdraw the ability to defer liability for CGT by investing in VCT shares from 6 April 2004. In favour of an enhancement, of equivalent value, to the incentives to invest through income tax relief;
- an additional temporary improvement in income tax relief from 20% to 40%; and
- increase the upper investment limit from £100,000 to £200,000 in any financial year.

RDA recommendation: Welcome review of Small Firms Loan Guarantee Scheme (SFLG) proposed in the Pre-Budget Report. Emphasise the need for Banks who operate the scheme to adopt consistent approaches to lending.

Government response: The Graham review is examining whether, through SFLG and other interventions, the Government is doing all that it can to help start-ups and small firms overcome the obstacles that they face when raising debt finance. The review issued in February a discussion document and

invited submissions from interested parties. The review is working closely with the main SFLG lenders and will examine, and if appropriate make recommendations regarding:

- the structure and rules of SFLG and their appropriateness to the scheme 's effective operation; and
- whether SFLG, as the Government's principal intervention in the supply of debt finance to SME, is sufficient to tackle the barriers faced by start-ups and small businesses in the current market.

RDA recommendation: Consider encouraging regional co-ordination and brokering of business angel networks by fiscal incentives for business angels to join such networks.

Government response: Business angels provide valuable growth capital and business mentoring for firms seeking small amounts of equity capital. The Government is keen to see greater levels of business angel syndication, which often takes place most efficiently at a regional level. Networks can encourage and facilitate both new entry of individual angels and greater levels of syndication. The Government is aware of the reported difficulties with the current tax incentives for collective angel investments, and will continue to discuss how to improve this regime with angels and other stakeholders over the coming months.

4. SKILLS PROVISION

RDA recommendations: Continuation of commitment to 'regional devolution' of skills planning and policy, but allow each region to develop its own structures, building on what it has already developed.

Government response: *Devolving decision making: 2 – Meeting the regional economic challenge: Increasing regional and local flexibility*, published today, sets out the regional and sub-regional variations in the skills of the current workforce and the attainment of those yet to enter the labour market. Recent studies conclude that these variations in regional skill levels are a major factor in explaining variations in their productivity, and are therefore critical in determining current and future regional economic performance. Improving regions' skills base is therefore a crucial component of the Government's regional productivity agenda.

The Government has put its support behind the creation of new Regional Skills Partnerships as a way to bring together the key stakeholders in regional skills delivery – RDAs, the Skills for Business Network, the Small Business Service, the local LSCs and Jobcentre Plus. Regional Skills Partnerships provide a real opportunity to create an integrated approach in each region, to increase employer demand for skills and to equip adults with the skills that employers need. The first Regional Skills Partnerships will be established from April 2004. It is for each region to determine the structure of the Partnership and how it operates to best meet its needs.

To provide genuine integration between the roles of different stakeholders and coordination of resources at a regional level, Regional Skills Partnerships must be sufficiently empowered to overcome real or perceived difficulties of joint-working which currently exist. The Government announces today its commitment to address any institutional barriers identified by the Regional Skills Partnerships to creating an effective and integrated approach to regional skills delivery, taking into account the balance with national policy.

RDA recommendation: Far greater devolvement to region of LSC budgets and policy (not just management).

Government response: The Government is announcing today in *Devolving decision making: 2 – Meeting the regional economic challenge: Increasing regional and local flexibility* where Regional Skills Partnerships agree that a pooled budget, aligned targets or changed planning cycles are necessary to achieve the objectives of the Regional Economic Strategy and the Frameworks for Regional Employment and Skills Action and to deliver their business plan in an integrated way, the Government will enable this, again taking into account the balance with national policy.

RDA recommendation: Creation greater regional flexibility in LSC, Jobcentre Plus and Connexions target framework

Government response: The new Regional Directors for the Learning and Skills Council will ensure that the LSC plays its full part in developing the RES and FRESA, and in shaping LSC funding and operations to support the agreed regional outcomes.

5. KNOWLEDGE TRANSFER

RDA recommendation: Need to provide certainty and permanence for Higher Education Institutions (HEIs) for the ‘third stream’ of HE funding to enable HEIs to invest in core services.

Government response: The “third stream” funding referred to here is the Higher Education Innovation Fund, currently in its second round. HEIs bid into the fund for knowledge transfer activities, up to a maximum of £2.4m per institution, or £3.25m if they are part of a collaborative bid. The second round of HEIF will allocate £187m in England over two years - 2004/5 and 2005/6.

The Lambert Review of business-university collaboration recommended that third stream funding should be substantial, permanent and allocated in a way that enables universities to make long-term plans for these activities. In responding to Lambert in Budget 2004 the Government is announcing today that it will build the Higher Education Innovation Fund as a permanent third stream of funding for universities in England to further build the capacity in the university sector for knowledge transfer. The Government will develop this policy as part of its ten-year investment framework for science and innovation. The Government’s full response to the Lambert Review will be produced by summer 2004, and published as part of the ten-year investment framework for science and innovation.

RDA recommendation: Need to regionalise the allocation of HEIF to help the co-ordination with regional innovation and science strategies – RDAs should be involved in decision on allocations of funds within their regions.

Government response: The Government has actively encouraged collaboration between HEIs in the second round of HEIF by providing a maximum of £2.4m for institutions that do not collaborate compared to £3.25m for those institutions who collaborate. A key innovation in the second round of HEIF compared to the first round is an enhanced role for RDAs in deciding HEIF allocations through:

- RDA involvement in developing proposals to ensure that gaps are filled, best practice is adopted, regional economic strategy is supported, and that third stream activities are joined up and integrated with other activities;
- RDAs either providing linked funding or helping HEIs to access it;
- RDAs contributing to the assessment process by ranking proposals through the Regional Advisory Group and by representation on the Advisory Board.

In considering the next steps for HEIF, the Government will be looking closely at universities' proposals for knowledge transfer coming out of HEIF2, and the RDAs' roles in shaping these.

In addition, in responding to Lambert in Budget 2004, the Government has announced an enhanced role for the English RDAs in strengthening business-university links. The Government believes that the RDAs are well-placed to promote business-university collaboration but recognises that they need the capacity and links to national innovation programmes to do this most effectively. The Government will continue to explore with RDAs and other stakeholders the best mechanisms for fostering business-university collaboration.

RDA recommendation: Regional HEIF should explicitly support "regional shared services", but with the best model determined in each region.

Government response: Lambert recommended that the Government should use third stream funding to support regional shared services in technology transfer. The Government has actively encouraged collaboration between HEIs in the second round of HEIF by providing a maximum of £2.4m for institutions that do not collaborate compared to £3.25m for those institutions who collaborate. The Government will make its final response to the Lambert Review in the ten-year investment framework for science and innovation to be published alongside the Spending Review.

NORTH EAST STATISTICS

The New Deal has been successful in helping more than 62,170 in the North East into work. This has helped employment in the North East rise by 2.5% and unemployment fall by 34.2% since 1997.

As a result of personal tax and benefit measures introduced since 1997, by October 2004 households in the North East will be, on average, £1,010 a year better off in real terms.

NOTES FOR EDITORS

Further details of Budget 2004 announcements can be found on the HM Treasury website: www.hm-treasury.gov.uk. Copies of Inland Revenue and HM Customs and Excise Budget Notes can be found on their websites at www.inlandrevenue.gov.uk and www.hmce.gov.uk respectively.

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HM Treasury www.hm-treasury.gov.uk

Inland Revenue www.inlandrevenue.gov.uk

HM Customs and Excise www.hmce.gov.uk