

SECRET



case 2
Prime Minister
The bids total
nearly £1200 m for
1987-88.

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9/6.

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From the Secretary of State for Social Services

The Rt Hon John MacGregor OBE MP
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ms 6 June 1986

John John.

PUBLIC EXPENDITURE SURVEY 1986: SOCIAL SECURITY AND DHSS ADMINISTRATION

I am writing under the revised guidelines agreed for this year's Public Expenditure Survey to give you details of the increased provision required for the social security programme and Departmental administrative expenditure. I have carried out my scrutiny of the social security expenditure situation from the basis of our reforms of the system which are now before Parliament. These reforms are of course important in themselves for the improvements which they offer; will give better control of expenditure; and are vital to our political position. I have therefore kept to an absolute minimum policy bids unrelated to them; the only one of any significance is the cost of resolving the problem over Invalid Care Allowance. But if our reforms are to succeed we must be as realistic as we can about the probable demands on the social security system and the scope for financing these demands out of policy changes of a politically damaging kind. This letter deals with these issues, and Annex 1 sets out the principal figures.

Benefits

Review Related Bids

We expect over the next few months to re-cost the Review measures in particular in relation to income support, family credit and housing benefits in the light of recent data and I wish to consider the position of the various groups in the light of that examination. We also still have to settle in E(LF) the future arrangements for assisting low income families with the community charge which will have significant distributional effects. But it is already evident from the Social Security Bill's passage through the Commons that some easements will be essential if we are to secure public acceptance of the reforms. For example, severely disabled claimants will suffer large losses as will some one-parent families. We have also identified some very minor changes which will make the operation of the social fund more acceptable. At this stage I can only register a provisional bid of £50 million for improvements to the package of review measures.

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Social Fund - start-up

There is a particular problem over the social fund's start-up costs. Loans will form a major element of the fund. Clearly, because of the timelag between the granting and recovery of loans it will be necessary to provide additional resources for the first year of its operation. The only alternative would be to curtail severely the number of loans made in that year. This would be impossible to justify and would get the new arrangements off to the worst possible start. I estimate that an additional £25 million will be required for 1988/89 to deal with this problem, but I should be able to cover this cost by savings on the uprating in 1988/89. The Social Security Bill provides for the main uprating to take place in the week beginning with the first Monday in the new tax year, rather than the week in which 6 April falls. In 1988 this will mean that the uprating will not take place until the week commencing 11 April, saving about £25 million.

Invalid Care Allowance

You are well aware that this bid stems from a probable, adverse judgement of the European Court and we are due to discuss the matter again shortly. We have not yet agreed what action should be taken, if any, to limit the expenditure consequences of the anticipated judgment but for the purposes of this exercise I have assumed that a recent work test will be introduced. I must reserve my position on the size of the bid until we have discussed further.

Minor Changes

These are very small indeed and I will not trouble you with the detail at this stage. I expect to find offsetting savings to finance them.

Housing Benefit Administration

Local authorities will incur significant additional expenditure in 1987/88 if they are to make adequate preparations for the start of the reformed housing benefit scheme and, in my view, the Government must be seen to be providing an appropriate level of support for these unavoidable costs. My best estimate at this stage is that I will need to bid for £30 million to cover this. We will be having detailed discussions with the Local Authority Associations but until these are concluded the figure must remain provisional. I suggest that initially we pursue this question in the context of RSG discussions, not least because the timetable on that front is tighter.

Administration

My bid on the Administration Vote consists of three main elements, normal work, reform implementation and operational strategy.

Normal work: when we reached agreement on manpower and money for normal work in 1986/87, the carry forward to future years was left open. The bulk of the bid is this carry forward. This line also has to reflect pay settlements over the period. I am not bidding for more than the assumed inflation rate but I must stress that we control neither the pay negotiations nor the settlement. This bid has to be judged against the background of two concurrent exercises: the complement review in our local offices and the joint study by our officials of the scope for

E. R.

efficiency savings. The results of these two exercises will not be available until well after the PES round and I suggest our officials discuss how this inevitable uncertainty can best be handled. For the purpose of the current estimates, leaving aside the interim costs of implementing the social security reviews, we have simply assumed the continuation of the agreed 1.4.87 figure for manpower of 96,750. You will recognise that at this stage I can give no guarantee that the results of these two exercises will in fact balance out.

Reform Implementation: I have shown separately my bid for the costs of implementing the current Social Security Bill. The 1987/88 figure given in Annex 1 - which must necessarily be subject to a degree of uncertainty at this stage - covers the staff costs of reassessing cases under the new rules and of training our local office clerks, plus items such as accommodation, the development of new computer systems, reprinting of leaflets and publicity. On the other side of the equation, there are administrative as well as benefit savings flowing from the reforms which are already apparent in the figures for the last two survey years. I believe these fully justify the initial costs. Indeed, the administrative savings alone would make this an attractive investment under the normal criteria, with an internal rate of return in excess of 10 per cent over ten years.

Operational Strategy: I have also shown separately my bid for the costs of implementing our operational strategy: again an investment justified by large future savings. Our officials are currently conducting the annual review of the strategy and the bids may have to be adjusted in the light of that exercise.

The details of these bids will be provided separately to your officials. I recognise that the consequences for the running costs total are very significant. A substantial part of this is very much an investment, however, more akin to capital expenditure - indeed, I believe many private sector firms would classify it as such. The underlying increase in running costs for the day to day work of the Department does come within the target at the end of the survey period, though it is slightly above it at the beginning. In practice, we could come within the target only by reducing our manpower requirement and the arguments against this are precisely those you found persuasive in February.

Forecasting changes

Annex 1 also records our current estimate of forecasting changes to the baseline. In the first two survey years, the economic changes are simply a reflection of changes in the underlying economic assumption provided by your Department, and of the significant increase in rents and rates in the current year. The large figure in the third year is a direct consequence of the artificial way in which the baseline has been created, without full provision for the benefit upratings which we are committed to make. In the last two PES rounds, it was accepted that provision for a full uprating should be treated as essentially an agreed change, and I assume this will be the case this year.

It is disappointing that despite the efforts of both our Departments to improve our forecasting methodology, we are still faced with uncomfortably large estimating changes. In part they arise because the new methodology is giving us early warning of increased

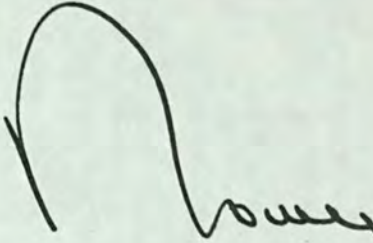
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expenditure; there appears to be a continuing upward movement in the number of people receiving benefit, in lengths of period in receipt of benefit and in entitlement, but further statistical information will be necessary to confirm this. Moreover, the figures underlying Cmnd 9702 were vulnerable to the limited availability of much of the basic statistical data following the 1984 dispute at Newcastle. It is now necessary to correct for this in the light of the information becoming available. Experience indicates that the figures for both the economic and the estimating changes are likely to change significantly as the PES round proceeds, and it would not be sensible to base discussion on the current figures, which are inevitably far from precise. I suggest that the forecasting changes in Annex 1 be regarded as for reference only at this stage, and that any substantive discussion be based on the next cycle of forecasts in August.

Offsetting savings

I have considered the scope for offsetting savings but, having just concluded an extensive review of social security provision, I am in no doubt that I could only find such savings by either announcing major changes to the new schemes before they have even begun or by making savings in those few areas not covered by the review, eg disability benefits. I attach an illustrative list of possible savings measures which my officials have identified and one has only to look down the list to appreciate that securing savings of this kind would carry a very high political risk indeed. Even then, the list is short of the sum which would be necessary to offset in full the increase in baseline expenditure. We have had experience of the political difficulties which a series of social security savings measures can produce and I am certain that to introduce the measures of the kind in the list would place us in even greater difficulties.

I am copying this letter to the Prime Minister and the Lord President.

Yours ever


NORMAN FOWLER

SOCIAL SECURITY - BENEFIT AND ADMINISTRATION BIDS

	£ million cash		
	1987-88	1988-89	1989-90
1. Baseline	42,458	43,834	44,930
2. <u>Benefit bids</u>			
2.1 Review related contingency bid	+11	+50	+50
2.2 ICA - recent work test	+50	+47	+41
2.3 HB start-up cost	+30		
3. <u>Administration bids</u>			
3.1 Normal work ¹	+147	+161	+181
3.2 Operational strategy	+42	+64	+32
3.3 Reform implementation	+93	-7	-22
TOTAL	373	315	282

Forecasting changes

economic	+250	+310	+645 ²
estimating	+550	+600	+1,140

Notes:

- This is the continuation of the sum already agreed for this year.
- £300 million of which is due to the way the baseline has been constructed for the final year.
- Two benefit bids are to be fully offset by savings and do not add to the total:

a) Social Fund - start-up	-	+25	-
b) Minor changes	+5	+2	+9

POTENTIAL SAVINGS MEASURES

PROPOSAL	£ million cash		
	1987-88	1988-89	1989-90
1. Offset occupational pension exceeding £35 against unemployment benefit for all age groups	-	40	45
2. Offset occupational pension exceeding £35 against unemployment benefit for those aged 55-60.	-	30	35
3. Offset occupational pension exceeding £35 against sickness benefit/invalidity benefit for those aged over 60.	-	90	95
4. Offset occupational pension exceeding £35 against sickness benefit/invalidity benefit for all age groups.	-	170	170
5. Defer abolition of retirement pension earnings rule by a further year.	-	-	100
6. Abolish 25p age addition for pensioners over 80.	-	24	24
7. Abolish Christmas Bonus.	-	114	114
8. No uprating of supplementary benefit additional requirements in April 1987.*	17	-	-
9. Increase available scale margin by 10p/50p in April 1987. (This is an offset against additional requirements for claimants in receipt of the long-term rate of supplementary benefit).*	10/50	-	-
10. Housing benefit - steepen rent taper from 29% to 33%.*	28	-	-
11. No child benefit uprating in April 1987.	80	80	80
12. No uprating of "unpledged" benefits in April 1987.	350	350	350
13. Unemployment benefit disqualification for claimants voluntarily unemployed - extend period from 13 weeks to 6 month/1 year.	-	110/160	110/160
14. Attendance Allowance - pay a reduced rate for children aged 2-4.	8	8	9

↑

15. Attendance Allowance - pay a reduced rate for children of all ages.	40	41	43
16. Widows - apply £75 earnings rule (as for retirement pensioners).	-	27	27
17. Apply an earnings rule of £100 to both widows and pensioners	-	100	100

* Note: savings from these measures are subsumed in review savings in 1988/89 and 1989/90.

