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Prime Minister

MLS 31/3

PRIME MINISTER

LONG TERM PUBLIC EXPENDIUTRE: SOCIAL SECURITY

This minute, which responds to your minute of 4 February, deals with the social security programme. The proposals in it have been discussed with Treasury Ministers.

There are three broad routes by which we could make a major impact on social security public expenditure totals:

across the board reduction in the value of social security benefits;

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contracting-out more responsibility for income support;

redefining the scope of public expenditure.

Across the board reduction in the value of benefits

There is no technical difficulty about achieving a substantial reduction in public expenditure by an across the board reduction in benefits. This could be done as a one-off exercise or by altering the statutory basis of uprating legislation. For some benefits, principally contributory benefits, such as retirement pension, main legislation would in any event be needed.

Having considered this option carefully however my conclusion is that we should not go further than we have already gone in amending the basis of legislation and so hold back the value of benefits. We have already done much to constrain the automatic growth in the value of benefits by amending the legislation, so that we now uprate benefits in line with prices, rather than the better of prices and earnings, and also by going over ~~/~~ to the historic method which will prevent unintended bonuses. The change to uprating by prices only already means a saving of £500 million a year in the programme. Moreover, if we had not done

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this the annual cost of the social security programme would be some £2 billion to £3 billion higher by the end of the decade.

But contributions would have been prohibitive.

Whilst we must keep a careful watch on the overall extent of social security spending, bearing in mind for example the development of the earnings related pension scheme, we must also recognise that if we do not uprate by more than prices we are already going to hold down the value of benefits compared to the standard of living of most (if not all) of those in work. We need to think carefully before we went any further in this direction. We would open up an unreasonably large gap between the living standards of pensioners and other long term beneficiaries and the rest of the community.

This already exists - millions do not have price protected pensions

The only point for early decision is what we say about our intentions on price protecting pensions in the next Parliament. You have separate minutes from the Chancellor and me on this, which set out our differing views.

Contracting-out more responsibility for administering income support

There are two main possibilities for contracting-out more responsibility for administering income support:

(a) through employers, following the examples of statutory sick pay (SSP), or contracting-out of the state pension scheme;

(b) through local authorities, following the example of housing benefit.

A. To employers

In principle it would be possible to consider following the SSP pattern, where employers pay the benefit and recover the costs from contribution income. This would not save resources generally but would lead to staff savings.

However, the statutory sick pay scheme does not start until next month (April). It would be better to let this scheme settle down and resolve any teething troubles before we take further initiatives in this field. We must accept that some employers, especially small

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businessmen, will take time to get used to the scheme and may initially be rather hostile to it. In particular, they will be concerned about having to pay National Insurance contributions on the statutory sick pay.

If experience shows that employers are able to cope satisfactorily with the statutory sick pay scheme and even see advantages in it from their point of view, it would be possible to take further initiatives along similar lines. There are three possibilities at least, though I should not like to underestimate the difficulties of implementing any of them. They are:

> replace the present maternity benefits (contributory maternity allowance, non-contributory maternity grant, maternity pay from the employer (reclaimed from the Redundancy Fund) and sickness benefit) by a single maternity benefit paid by the employer. This would reduce public expenditure by £200 million in 1984/85;
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> extend statutory sick pay to 28 weeks, thus abolishing sickness benefit. (After 28 weeks, invalidity benefit replaces sickness benefit.) This would reduce public expenditure by £300 million in 1984/85;
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> make employers responsible for the industrial injuries scheme. This would reduce public expenditure by £500 million in 1984/85. Possibly employers could themselves contract-out the administration to insurance companies, as they did with insured pension schemes.

The Chief Secretary and I have agreed that officials should study the possibilities in more detail.

No need. Employers already bear a big enough burden M

B. To local authorities

It would also be possible to contract-out administration of social security benefits to local authorities, who will administer housing benefits from next month (April). But I could not recommend this course, since the main options would be non-contributory benefits like

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supplementary benefit. It would be much more difficult to control expenditure on these benefits if they were administered by local authorities. Similarly it would be more difficult to control staff numbers.

Redefining the scope of public espenditure

We are more rigorous than most countries in classifying transfer payments as public expenditure. We could make a nubmer of changes in the classification of social security payments if we so wished. The possibilities are examined in the annex to this minute, though I ought to say that while the Chief Secretary is ready to consider any proposals we make, he does not regard this as a promising approach.

Conclusions

Of the three routes I have examined only the first would reduce the extent of transfer payments through the social security system. The second route would reduce the direct role of the state while the third route would primarily, though not solely, be a matter of presentation. While neither the second nor third route would reduce the resources involved, each could be valuable demonstrating that we were determined to ensure that limits were placed on the role of the state in direct income maintenance.

I am copying this to the Chancellor of the Exchequer, the Chief Secretary and Sir Robert Armstrong.

31 March 1983

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ANNEX

REDEFINING THE SCOPE OF PUBLIC EXPENDITURE

Definitions of public expenditure vary from country to country. Our community partners tend to be less strict - for example, some do not count contributory benefits as public expenditure.

If this route were pursued, there would be a number of possibilities for excluding social security expendiutre from public expenditure totals:

(a) exclude all National Insurance benefits (roughly 60 per cent of social security expenditure), but include the Treasury Supplement (13 per cent of contribution income);

(b) If (a) were not done, exclude just the earnings related additional component to retirement pension on the grounds that it is the equivalent to an occupational pension;

(c) exclude child benefit on the grounds that it is a tax credit;

(d) treat all housing benefits (not just rate rebates) as revenue forgone rather than public expenditure. Supplementary benefit payments to owner occupiers in respect of other housing costs could be treated in the same way.

Redefining public expenditure need not be seen just as a matter of presentation. What is counted as public expenditure does have a significance in itself since the size of public expenditure in relation to overall Government income and outgo can alter the perception of the country's financial structure and policies. In relation to social security specifically, the apparent size of the central provision of income maintenance may also influence perceptions of financial structure and policies.

cc NU

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Prime Minister[2]

MES 31/3

Prime Minister

LONG-TERM PUBLIC EXPENDITURE: HEALTH ASPECTS

1. Your minute of 14 February requested a report on the contributions that our programmes might make to a substantial reduction in public expenditure in the longer term and referred back to the work already done for the five-year forward look. My response to the forward look recorded the changes in demography and medical advance which give rise to pressures to maintain real expenditure growth on health services. I also described the initiatives I have already taken to contain these demands on public expenditure by securing more effective use of resources and better co-operation between health authorities and the private and voluntary sectors.

2. I have now, in consultation with the Chief Secretary and other Health Ministers, given careful consideration to ways in which we might provide further savings by raising income from charges, privatisation and encouraging the private sector through fiscal concessions. In carrying out this review we have necessarily looked at a number of very difficult and controversial measures. This report concentrates on options which we can be - and are - pursuing now, and those which I think should be ruled out altogether. There are other possibilities, notably in the general area of charges, on which detailed work could be quickly carried through if the necessity arose, but which are unattractive politically. I see little purpose in commissioning further work on these proposals at this stage, as the necessary political decisions could be taken and then implemented with little delay if and when the need for them arose.

3. Measures currently in hand, which I propose to take forward rapidly, include:

i. the independent review of the general ophthalmic services, announced last year. It will examine and review the structure, administration and financing of NHS ophthalmic services, and consider the role of the NHS in the provision of those services.

ii. a review of the scope for achieving savings on the drugs bill beginning with the recently announced review of the Pharmaceutical Price Regulation Scheme;

iii. issues of effectiveness and economy in prescribing by general practitioners and the possibilities of increasing generic substitution which are being pursued in the consultations now underway on the Greenfield Report;

iv. with the Inland Revenue I am looking at the possibility of fiscal help for private sector provision for the over 65s. Many people who were insured as working adults, perhaps through employer schemes, have to abandon such insurance when they retire because of the rapid increase in premiums required to cover their increased risk.

4. Another idea which I should like to follow up when I have been able to consider it in the light of Roy Griffiths' enquiry into NHS management, is that of an experimental contract for the private management of one or more NHS

hospitals. This is an approach which has been adopted in some hospitals in North America and in the private sector in this country. It would supplement the measures we are taking to make better use of resources within the NHS and which I set out in my December report.

5. I would rule out absolutely any attempt to levy charges on patients in hospital or for registration or consultation with a general practitioner. In practice they would subject the patient to charges at a point at which he would often be particularly unable to afford it, and they would act as a disincentive to seeking necessary treatment. Such charges could also require complex administration in operating a wide range of exemptions. Nor should I wish to pursue any idea of charging patients the full cost of treatment, whether in hospital or through general practice, with subsequent reimbursement. The evidence from France does not indicate any reduction in demand and with the administration costs this idea could actually increase public expenditure. These proposals as a whole are therefore of dubious practical value, but are politically very dangerous. The Chief Secretary wishes to keep the options open but I see no alternative to repeating the pledges against them which you gave in 1979 and 1980. Trying to keep our options open will merely arouse suspicions and feed allegations that we intend to introduce such charges.

6. Rising demand and public expectations make it unlikely that we will achieve substantial reductions in expenditure on the NHS overall, but we have to bear in mind that tight financial control has kept the level of health care spending well below that in other industrialised countries. The proportion of GDP which we spent on health services (public and private) in the UK in 1980 was 5.7 per cent compared, for example, to 8 per cent in France and Germany and 9.6 per cent in the United States. Next year the growth in resources financed by the tax payer will be 0.7 per cent or less depending on inflation and the Chief Secretary, and I have agreed on rough planning assumptions of about ½ per cent a year for the future. If we keep expansion to this rate, we should be saving £1.4 billion at the end of ten years compared to the growth rate in this Parliament.

7. I am also copying this letter to the Chancellor and the Secretaries of State for Wales and Scotland.

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31 March 1983