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3A-H Prime Minister².

AA.

You may like to see these before next week's meeting.

Reference E 0569

PRIME MINISTER

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10/5 3/6

with PAB

National Health Service
Meeting of Ministers 7 June 1988

Paper by Secretary of State for Social Services dated 3 June 1988
Minute by Chancellor of the Exchequer dated 3 June 1988.

DECISIONS

The purpose of this meeting is to consider what should be done to encourage the growth of the private sector in health. At its meeting on 9 May the group agreed that it was desirable to encourage such growth. It asked for the further papers which have now come forward to help it decide how this could best be done.

2. The main questions arising on the papers are:

- Should there be tax relief on private health insurance premiums paid by the elderly? This was identified as an interesting option at your last meeting. One argument for it is that the elderly find it hardest to arrange private insurance and have to pay much higher premiums if they do. It should also be less repercussive. The Chancellor does not oppose this option. It may be that it can be readily agreed in principle.
- Should private health insurance premiums paid by employers no longer be taxed as a benefit in kind? Such a concession was seen as another option at your last meeting. The Chancellor argues against it on the ground that there would be a high deadweight cost, and that there would be strong pressure to extend it to other private health insurance premiums and perhaps to private spending on education. Mr Moore's paper says that in his view fiscal incentives are important in encouraging the private sector. The case for a tax relief going more widely than the elderly could therefore be the most contentious subject at the meeting.



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- Should there be a form of contracting out from the NHS, under which, in return for some fiscal concession, those with private insurance would be unable to receive specified treatment from the NHS (unless they paid for it). The Secretary of State earlier argued for such a system. The Chancellor has argued against it, mainly on grounds of deadweight cost and repercussiveness. The group has not yet come to a final conclusion about it, but found the tax concessions more attractive. The Secretary of State has now mentioned the option again, as one to be reconsidered if no tax incentives are given on company scheme premiums.

- Can the Government take any other action to promote a mixed economy for health? Mr Moore's paper lists some areas where improvement is possible, and suggests that officials should prepare an 'action plan'. Not much progress seems to have been made in identifying what more might be done and you may want to agree with the proposal for an action plan.

In short, the main subject for the meeting is likely to be tax concessions for the private sector, with the main argument being whether they should go beyond the elderly.

ISSUES

3. The DHSS paper refers to the rapid growth of the private sector. The attached chart from the earlier DHSS paper (HC4) shows however that growth in the private sector was very rapid in the late 1970s but has been much slower in the last few years. You may be interested to ask why this should be so. Does it create a case for a special effort to encourage further growth? Mr Moore argues in his paper that without some fiscal stimulus there is unlikely to be a major expansion of the private sector.

Tax relief for the elderly

4. The Chancellor describes a scheme under which:



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- Tax relief would be available only at the basic rate.
not - at basic rate
- It would be given under a system, like that operated for mortgage interest, under which the taxpayer pays premiums net of relief and the relief is then paid to the insurer by the Inland Revenue. This means that all pensioners will benefit from the relief, whether they pay tax or not (the majority do not) and that the system will be simple to operate and make minimum demands on Inland Revenue manpower.
- The relief will also be available on premiums in respect of the elderly but paid by younger people. This will encourage families to provide for the health care of their older members.

These proposals seem generally sensible except that you may want to ask whether restriction of the relief to the basic rate might be taken as a precedent for mortgage interest relief.

5. More generally, the arguments for tax relief for pensioners are:

- Private medical insurance for the elderly has been slow to develop. This is therefore a part of the market where a tax incentive would be especially desirable.
- It might encourage people to join schemes before pension age if they were no longer faced with such a steep increase in premiums at that age.
- It is not expensive - a deadweight cost of only £25m a year - even without making any allowance for NHS savings.
- It should not be unduly repercussive. For example, it could not easily be used as a precedent for education.



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The group may therefore be able to decide in principle that there should be tax relief for private insurance premiums paid in respect of pensions^{or}, broadly along the lines described by the Chancellor.

Tax concession on premiums paid by employers

6. This will be much more contentious. The proposition was that premiums paid by employers should no longer be taxed as a benefit in kind in the hands of employees. The Treasury oppose it because:

- It would be repercussive. They say it would be very hard to resist pressure for tax relief on premiums paid by the self-employed and by employees not in company schemes. There could also be pressure for a similar concession in education.
- It would not encourage the expansion of insurance schemes, since the employers who provide them would get no benefit from tax relief for the employees.
- It would be poor value for money. Tax relief for private premiums which would have been paid anyway and the difficulty of making savings in the NHS mean that the share of health care financed privately would not rise, and might even fall.

Yes it would - employers would be more likely to demand them.

7. As to the danger of repercussions, it may well be that it would be difficult to give relief for premiums paid to employers and to deny it for those paid by the self-employed or by employees. The question is perhaps whether relief should be available for private health insurance premiums generally. This would also be more effective in encouraging the growth of private insurance, although it would of course also be more expensive - in his paper of 22 April the Chancellor estimated the cost of general relief on premiums as just over £200m.



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8. As to the value for money criticism:

- Are the Treasury pessimistic in supposing that there would be no reduction in NHS expenditure if there were an expansion in the private sector? In principle, the PES allocation for the NHS could be fixed lower, or not increased so much, because of the higher private sector contribution.

- Even if a tax incentive for the private sector were not good value for money in the short run, is it worth incurring a shortterm disadvantage for the sake of a long-term change in the culture?

Contracting out

9. Mr Moore says in his covering minute that if the group concludes against changing the present tax treatment of company schemes it might reconsider the possibility of a system of contracting out limited to cold elective surgery. This is also an option which has been mentioned in public debate.

10. Contracting out has usually been thought of as providing a rebate on a health contribution for those who undertake to rely on the private sector for specified treatment, most often cold elective surgery. The Chancellor earlier argued against it on the ground that it would not be cost-effective in raising the private sector contribution to health finance. The arguments are the same as those he used against a general tax concession on insurance premiums: there would be a heavy deadweight cost, and it would be difficult to make cuts in NHS expenditure.

11. If the group favoured general tax relief on insurance premiums, you would probably not want to pursue the idea of a contribution



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rebate as well. If the group does not favour general tax relief you will want to decide whether to take up Mr Moore's proposal to reconsider contracting out. In that case, a detailed study of a possible scheme will be required. You may want to set this work in hand only if you consider contracting out sufficiently attractive in principle.

12. It might be possible to tie contracting out to tax relief rather than a contribution rebate. The relief would then be given only on premiums paid to schemes whose members relied entirely on the private sector for the treatment specified.

Other measures to promote a mixed economy

13. Mr Moore's paper describes a number of areas in which there could be better cooperation between the NHS and the private sector, or in which the private sector could improve its own performance. The paper does not suggest what the Government should actually do to improve matters, and you may therefore think that detailed discussion is not necessary at this stage. Mr Moore's covering note proposes that officials should now be asked to prepare an 'action plan'. You may wish to ask for such a plan to be prepared quickly.

14. The annex to the paper suggests that costs in the private sector are generally higher than those in the NHS. You may want to discuss why this should be so, and whether there is any risk that expansion of the private sector, or closer working with the NHS, would tend to drive up health costs. The annex also shows however (paragraph 6) that geriatric care is much cheaper in the private sector than in the NHS. You might ask for the further work to look particularly at the scope for using the lower costs of geriatric care in the private sector.

Next Steps

15. You have already agreed that the next meetings of the group should deal with the following subjects:



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Week beginning 27 June.

1. Financing hospitals, especially Chief Secretary's proposal for rewarding the best performers.
2. Self-governing hospitals and capital allocations.
3. The profession, especially consultants' contracts and other pay and management issues.
4. Audits.

Week beginning 11 July

The overall package.

16. If you do commission work on contracting out or on the 'action plan' for developing the private sector, it might be made ready for the discussion of the overall package in the week beginning 11 July.

G W MONGER

Cabinet Office
3 June 1988

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CHART 1

PEOPLE COVERED BY PRIVATE INSURANCE

