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Policy Unit

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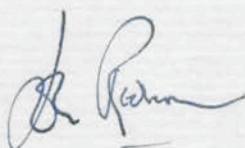
PRIME MINISTER

I attach a brief for Thursday's DHSS meeting.

I have followed the numbering of the DHSS Green Book, as that is comprehensive. The Agenda paper leaves aside several important issues which may need review. I have also given you the Agenda references where the Agenda covers that topic.

Unfortunately the Agenda does not follow the same numbering system as the Green Book.

Would you rather our brief was recast according to the Agenda numbers?



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JOHN REDWOOD

SECRET

PRIME MINISTERHEALTH AND WELFARE

In 1983/4, we will be spending £36 billion on social security, and another £15 billion on health, a total of more than £50 billion - over 40 per cent of Public Expenditure. The Green Book suggests that the rapid growth rate of 5.1 per cent per annum over the last decade will reduce to 0.9 per cent this Parliament. This will require considerable effort and improvement in DHSS control over their expenditure. The aim of the system should be:

- (a) to provide a basic state retirement pension;
- (b) to provide a good quality health service with care on demand, free of charge to the user;
- (c) to encourage private health and pension provision as incomes and expectations rise;
- (d) to protect the disabled and those who have been driven into poverty by unavoidable circumstance;
- (e) to avoid turning the social security system into a shirkers' charter by paying those who could or should fend for themselves.

A. THE HEALTH SERVICEAgenda 2, 1a and 1b

1. In the hospital sector (2.3-2.7, Green Book), we should not go back on our pledge to maintain a free service. The Griffiths reorganisation presents an opportunity and the possibility of another disaster. We should expect to see:

- (a) the rapid appointment of a Chief Executive for the NHS of a suitable calibre;
- (b) we should not expect to see early appointments of managers in the Districts and hospital units until the Chief Executive has been appointed and can express his views on how these appointments are to be made. If too many appointments are made by jumping the gun, we are likely to end up with promotions for unsuitable people already in the system, which will mean salary rises without bringing any management benefits (remember the gravy train on reorganisation of local government in 1973-4);
- (c) more rapid progress in contracting-out the basic support services (cleaning, laundry, catering);
- (d) a vigorous attack upon the enormous drugs bill. Whenever I visit people in hospital, I am struck by the freedom and enthusiasm with which drugs are administered. It is difficult often for a patient even to resist a sleeping pill when they would never dream of using one at home;

- (e) more use of spare hospital space to encourage private provision of extra facilities (additional refreshments, retailing of flowers and gifts etc) to generate income from rents for the hospitals;
- (f) the £50 million required per annum to clear the waiting lists should be authorised out of these savings, publicised, and a drive launched to remove the backlogs: they might even be persuaded to do it for less, as there should not be such long waiting lists given the cost of the system.

2. Family Practitioner Services (2.8-2.12, Green Book; Agenda 2.2). The GP services are justified on the grounds that:

- (a) the GP acts as a necessary postbox for people with more serious conditions;
- (b) the GP can solve a number of medical and related problems;
- (c) the GP is a trusted member of the community, and as such is politically popular.

The danger with the GP service is that there is little control over costs. The move towards group practice and community health centres has been used as a means of reducing doctors' working hours to a greater extent than as a means of improving efficiency and quality of service. We need to ensure that:

- (a) there are tight controls over the number of GPs, as proposed by Binder Hamlyn;
- (b) the medical schools do not produce more doctors and dentists than can be absorbed into the NHS system and the private sector on reasonable forecasts over the next 10 years;
- (c) there is a renewed drive to deal with the twin problems of over-prescribing drugs by the GP and the choice of unreasonably expensive drugs when cheaper generic drugs would be as good;
- (d) Community Health Centres aim to handle as many problems as possible that would otherwise be routed to a hospital, like the treatment of simple emergencies and the carrying out of basic health tests.

3. Parallel Imports. Around 10 per cent of the total ethical drug market in the UK is accounted for by so-called Parallel Imports. These are drugs imported from overseas and sold to the distributors and chemists at much cheaper prices than if they bought the same drugs direct from the UK manufacturer. The NHS still pays the full UK price, with the imported, distributor and chemist pocketing the difference as extra profit.

The differences can be large. The table below gives examples for leading UK and foreign drug company products.

<u>Company</u>	<u>Product</u>	<u>Treatment</u>	<u>Size</u>	<u>UK Trade Price</u>	<u>UK Import Price</u>	<u>Discount</u>
Glaxo	Ventolin	Anti-Asthmatic	One inhaler	£3.00	£2.06	32%
	Trandate	Anti-Hypertensive		£18.94	£15.16	20%
ICI	Inderal	Cardiovascular		£39.70	£31.36	21%
	Nolvadex	Anti-Cancer		£70.66	£56.53	20%
Beecham	Amoxil	Antibiotic	100x 250mg	£17.12	£13.70	20%
Boots	Froben	Anti-Inflammatory		£39.12	£31.30	20%
Fisons	Opticrom	Anti-Allergic	10ml	£4.50	£3.37	25%
Smith Kline	Tagamet	Anti-Ulcer	500x 200mg	£74.15	£65.25	12%
Merck, Sharp & Dohme	Aldomet	Anti-Hypertensive	500x 250mg	£27.23	£21.78	20%

The trade in parallel imports is likely to grow as the margins are so attractive to distributors. If this happens, the NHS should review its purchasing policy with a view to cutting its prices for the drugs to allow for cheaper import sources. The UK manufacturers are opposing the practice of parallel imports on the grounds that it will reduce their profits and endanger their R&D. However, it will become impossible for the NHS to go on paying high prices for drugs that are in practice sourced more cheaply (there could be a PAC enquiry which would cause discomfort). The savings could be well over the £65 million projected so far from the reduced rate of return formula announced recently.

The Binder Hamlyn Report noted the problem of the drugs bill, but did not investigate it thoroughly. It suggests that the Pharmaceutical Price Regulation Scheme should be adapted through the provision of more regular checks and information. The pressures on the pharmaceutical marketplace are likely to prove far better guardians of the public purse: a more open UK pharmaceutical market will cut costs for the NHS significantly.

Charges for NHS (Agenda 2.2b). The subject of charges has always been an explosive one. Any attempt to widen the range of charges would cause a major row and give the Kinnock campaign against Conservative welfare policy new momentum.

However, charges can be increased as under current policy. It is also possible to increase the numbers of people who voluntarily pay for a better standard of service, by offering them the choice. In the case of spectacles, most have chosen to pay more for a better product. In hospital, franchise catering outside the main meal service might attract considerable support, and could be privately run and financed.

Remuneration for Contractor Professions (Agenda, 2.2c). The row has blown up because some chemists have objected to the benefits to others of large discounts from pharmaceutical wholesalers. Pharmacies are remunerated on the basis of costs or expenses calculated as an average. This encourages the drive for efficiency and better purchasing, but can lead to allegations of overpayment for the larger or more astute.

A law suit on this subject is likely to go against the DHSS/NHS and the DHSS therefore wish to include clauses in their forthcoming legislation to legalise current practice.

They could also use the opportunity to review the basis of remuneration and clawback in the light of the large discounts and the parallel importing problem examined above.

The Private Contribution (Agenda 2.3). Provident insurance currently attracts Corporation Tax relief for company payments. Companies also benefit from block discounts and therefore growth has been most rapid for employer schemes.

Expansion of private insurance increases the flow of funds into the health sector, whilst leaving it to individual choice. Granting income tax relief would increase the rate of take-up, but would add another distortion to our grotesquely complex tax system. Private schemes are likely to grow quite rapidly anyway under the impetus of company relief. Shouldn't the public sector publicise its block scheme insurance to encourage a bigger take-up of those insured schemes in the public sector? There is a low level of awareness of these schemes in the Civil Service.

B. SOCIAL SECURITY (Agenda 3)

4. Child Benefit (2.13, Green Book). Child Benefit is costly - £4 billion this year. It goes to far too many people, and is the least popular benefit. It is non-contributory and unselective, a combination which people do not readily understand, and many disagree with. There are several ways of tackling this problem:
- (a) The Benefit could be frozen in cash terms throughout the life of this Parliament. There would need to be compensating adjustments in some of the other benefits going to low-income families, but these could be targeted more accurately, and therefore cost less overall.
 - (b) The Benefit could be increased but brought into the tax net. This would have the advantage of perceived justice, and would mean that the mother would still receive the benefit, whilst the father would pay the tax in the normal household.
 - (c) We could go back on our commitment to make no change in structure, and abolish the Benefit, replacing it by a beefed-up benefit for poorer families through SB and FIS. This would represent the largest saving of all in cash terms, but care would be needed in presenting the case in view of the previous commitment; and in constructing the new benefit, as it could exacerbate the poverty trap problem. Tax relief of at least £2,000 million could be granted at the same time as the pay-off for change.
 - (d) The two-tier child support system. The universal basic tier would be frozen at present levels, and the second tier would be paid to all unemployed families and working families now on FIS.

The best change, if the priority is simplification and tax reduction, is abolition. To avoid the row this would entail, the best option is to freeze the benefit.

Agenda 3d (Action)

5. Family Income Supplement (2.15, Green Book). Not one of the most expensive benefits, it does go to poorer families. It should be reviewed as suggested by the DHSS to lower its unemployment trap effects.

Agenda 3b (Issues)

6. Housing Benefit (2.16, Green Book). The recent review has already aroused protest, but it is important to reduce the numbers receiving the benefit who are already in receipt of reasonable incomes. The DHSS should press on to ensure the payments are concentrated on the lowest income earners, and should reinforce the case in favour of the changes they are making by giving examples of those who are better off under the revised scheme. Care should be taken to avoid penalising the poor.

7. Maternity Benefits (2.17, Green Book). The objective of combining the allowance with the pay in a single benefit paid by employers is sensible. It will be opposed by the CBI and others as another increase in employer burdens, and by pressure groups who could see it as another disincentive to employers to take on women employees in their 20s and early 30s.

The earnings-related component of maternity pay is generous and could be eroded.

Agenda 3c (Action)

8. Pensions (3.1-3.4, Green Book). We should retain the basic state pension and upgrade it in line with prices as pledged in the Manifesto. In view of the sharp real increase in pensions in the 1979-83 period, and in view of the general public expenditure pressures, we should aim to hold the pension steady in real terms for the next 2 financial years, beginning in April 1984.

Private sector pension schemes can be encouraged in two major ways:

- (a) Abolition of State Earnings-Related, forcing private provision.
- (b) Giving the employee control over the unitised value of his pension assets.

The advent of portable pensions (3.4, Green Book; Agenda 3c) would encourage self-reliance and would give the average pension scheme member (there are 11 million) direct control over an average £11,000 of assets already saved on his behalf in occupational schemes. It would represent a great advance in wealth ownership, and expand personal freedom and responsibility. It would also encourage more people to save for their retirement if they can see the fruits of their labours in the rising value of their own savings.

The State Earnings-Related Pension Scheme (3.9,3.10 Green Bk; Agenda 3c). This Scheme will prove too expensive. It is the ideal target for encouraging private provision in preference to public, and should be abolished before too many vested interests are built up. This would force more employers and employees to set up private schemes.

The Scheme could be abolished without too much dissent, as the vested interests that have so far been built up are quite modest. The Opposition would naturally make capital out of the

cancellation of a scheme to which we are pledged, and the abandonment of the bipartisan policy of pensions geared to earnings. We could, however, counter with a vigorous presentation of the opportunities for occupational pension schemes and for portable pensions.

9. The Problem of Elderly People (3.6-3.8, Green Book). The correct answer for all but the very infirm should be care in the community, preferably in their own homes. This has been the trend of policy in recent years, but the trend needs to be strengthened. Far too many old people are provided with permanent places in hospitals when they would be better off at home with home support services and the community around them. It would also be cheaper.
10. Other Dependent Groups (Section 4, Green Book). The disabled deserve as much help as we can afford. The record of the 1979-83 period in increasing the real value of many of these benefits was good. We need to ensure that help does go to those in need in this category, and to show compassion to those whose lives have been ruined by accident or disease.

The case of the World War widows who feel they deserve as good a deal as the Falklands widows could also be re-examined when uprating is under discussion. Well-publicised help to such groups has obvious political attractions when cuts are being made elsewhere in bigger spending areas, in addition to the humane consideration.

11. Unemployed (Section 5, Green Book; Agenda 3a Outstanding Issues). The review of the relationship between Unemployment Benefit and Supplementary Benefit should be encouraged. Two sets of offices are involved, and some streamlining might be achieved. It is important that any solution should not lose sight of the need to reduce the unemployment trap and to preserve a link between benefit and the search for a job.
12. Tax Credits (Section 6.4, Green Book). Now is the time for the Government to decide whether it sees any merit in this approach or not. Discussions are under way to see if the DHSS and the new Inland Revenue computer systems are compatible.

The best answer to the unemployment and poverty traps is to raise the tax thresholds by succeeding in lowering public spending and cutting income tax.

As part of that drive, the reviews of social benefits should be designed to simplify the benefit payment and assessment system, and to concentrate on those in need. Means-testing is a necessary part of the system, but the number of separate means tests should be reduced as benefits are simplified.

Meanwhile, tax reduction and reform should press ahead separately. Any attempt to unite the two could result in a costly auction of promises as the Government came under fire for having a "secret Manifesto" after all.

13. The Contributory Principle (Section 6, Green Book)

The contributory principle which underlay the original 1945-50 welfare state is a sound one and is well understood by most of the electorate. In order to reaffirm the contributory principle, there would be great merit in renaming one half of the income tax as "contributions towards the National Insurance Fund". People would then see the true cost of insuring for the benefits they will be collecting. The contributory principle associates in people's minds the cost with the benefit, and the pooling of risk across the whole population is a sound and sensible mechanism.

Conclusion

If these measures were adopted, and tighter controls exerted over spending, we might be able to halt the spending juggernaut. It is horrifying to see that spending is already £500 million higher than the 18 October forecast for 1984/5 before that year has even begun. The Chief Secretary is right to ring the alarm bells.

However, it is also vital that in our management reorganisations we achieve better delivery of a better service, which can be done for the £50 billion which is available. There are also one or two pockets of genuine poverty which need greater relief than they are currently receiving. For example, war widows who lost their husbands in wars other than the Falklands get an extremely raw deal, and feel even more bitter now that the Falklands widows are being looked after relatively well. The Government can present itself as one which cares and is prepared to use public money for the relief of genuine

hardship. It should also reduce waiting lists at hospitals in a concerted drive. Some indiscriminate benefits currently paid on a non-contributory basis undermine the amount of resource available for those in need, and undermine Government credibility about its belief in self-help. Given the pledges on state pensions and other benefits, the Government has little option but to tackle the difficult problems of Child Benefit and Housing Benefit. This will cause a major row, and should only be undertaken to achieve major cash savings.

The greatest scope lies in pensions. Radical action in introducing portability and cancelling the State Earnings-Related Scheme before its costs and vested interests build up could be popular and economical. It would represent the greatest shift in state/individual provision, and in individual wealth ownership, at the expense of institutions and the state, that your Government has ever undertaken.



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