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DEPARTMENT OF HEALTH & SOCIAL SECURITY

Alexander Fleming House, Elephant & Castle, London SE1 6BY

Telephone 01-407 5522

From the Secretary of State for Social Services

The Rt Hon Patrick Jenkin MP
Secretary of State for the Environment
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

1 May 1985

Dear Patrick.

Thank you for your letter of 26 April which we discussed yesterday. Before turning to the substance of the issues you raised, I feel I should put on record (as I believe you now recognise) that my proposals on the treatment of water rates and mortgage interest were in no sense brought forward at the last minute. They were clearly presented in my first report to MISC 111 at the beginning of February and your officials were made aware of them.

On water rates, I recognise that decisions you make to increase water charges faster than prices will be more difficult to defend if you cannot rely on 3 million supplementary benefit households being fully insulated from the cost. But I believe we were agreed yesterday that to retain water rates as the only individual element in the assessment of income support would be quite unjustified. It would destroy the alignment between income support and housing benefit and would be a first step away from the new simpler structure and back towards the complications we are now trying to dispose of.

My proposal - to move from individual reimbursement of 100 per cent of actual water charges for those on supplementary benefit to the inclusion of the average amount within the new income support scale rates - will, of course, have a transitional effect on individuals as will many other parts of the reform package. But it needs to be kept in proportion. Water charges represent on average less than 5 per cent of the scale rates (leaving aside additional payments for housing costs). Only 11 per cent of those having their water rates paid face charges of more than 50p above the average which will be included in the scale rate. Water rate increases also feed through into the RPI and hence into the uprating of benefits and the impact of the sort of increases you are committed to are equivalent to only 5p a week on average water charges. Finally, I can confirm that our intention would be to use all the resources going into the payment of individual water charges at the time of changeover to increase the scale rate - we would not expect to make savings from the change.

F.R.

As to mortgage interest, I accept that the building societies will be strongly opposed to my proposal that those on income support should not get help with mortgage payments for the first six months (beyond the 30 per cent help they get automatically through MIRAS). Nonetheless, I believe the arguments for the proposal are strong.

At present those in work get no extra help with mortgages even if they are on low incomes whereas those out of work get 100 per cent help. This provides a strong disincentive to the unemployed home owners taking on low paid work and can make unemployment or redundancy unduly attractive to those in lower paid jobs. We should do something to reduce that effect.

The Housing Benefit Review team recognised the inequity of this and considered whether housing benefit might not be extended to mortgages. I have firmly rejected that suggestion: it is not our aim to encourage home-ownership simply to have those buying their houses pass back much of the financial responsibility to the State.

My proposal to place the responsibility for dealing with short-term mortgage problems on the individual and his building society rather than the State is an important but limited step. It would substantially reduce the disincentive problems I have mentioned. It is crucial to my proposals to end the overlap between the new unemployment benefit and supplementary benefit; if mortgage interest is payable for the first six months, then anyone with a mortgage on the short-term unemployment benefit scheme would become eligible for income support as well. The proposal also produces worthwhile savings.

Yet the real impact on individuals and building societies would be limited. There are at present some 87,000 people on supplementary benefit for less than six months who are receiving help with mortgage interest, out of a total case load of 4½ million and one-quarter million getting mortgage interest paid. The change in policy would apply only to new cases arising in 1987.

As far as the building societies and their borrowers are concerned, the effect would be an interruption of mortgage interest payments of, at the maximum, six months. That would add about 5 per cent to the subsequent debt and repayments. In many cases it would be less since 70 per cent of spells of unemployment last less than six months in any event. Alternatively, the individual can insure his mortgage payments against sickness or unemployment for the required period at a cost well below 5 per cent of the payments. Given that the change would represent not a cash loss to the building societies but a cash flow change of well under 1 per cent of their total interest payments, I think the danger of building societies taking action to repossess is slight.

I recognise that there could be some effect on our drive to extend home-ownership. But the purpose of that policy is not just to give people a stake in their own housing but also to encourage them to take responsibility for their own affairs. We should not be encouraging people to take on more than they can handle or to believe that the State will automatically bale them out if they do.

F.R.

Finally, we discussed briefly the proposal to change the arrangements for reimbursing local authorities for housing benefit expenditure. I think we are agreed about the intention: to continue the same level of central government payments to local authorities at the time of changeover; but thereafter to restrict repayment based on actual expenditure to 80 per cent, with the remaining 20 per cent being subsumed within the RSG and controlled by GREAs in order to give authorities an incentive to control expenditure. We agreed that our officials should continue their discussions on this with the Treasury. We also agreed that the Green Paper should make clear our intentions on the principle but promise discussions with local authorities on the detail.

I am copying this letter to the Prime Minister, other members of the Cabinet, the Chief Whip, the Paymaster General and Sir Robert Armstrong.

Yours ever,

NORMAN FOWLER

-1 MAY 1985

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'BURDEN' OF PHASING COMPULSORY PENSION INTRODUCTION OVER 3 YEARS

'Burden' is measured as in Chancellor of Exchequer's letter of 22 April 1985.

1987-8	£million	
Private sector employers	150	Loss
All employees	200	Loss
Self-employed	-100	Loss
PSBR	300	Loss
TOTAL BURDEN	750	Loss

1988-9	£million	
Private sector employers	200	Loss
All employees	250	Loss
Self-employed	300	Loss
PSBR	450	Loss
TOTAL BURDEN	1200	Loss

1989-90	£million	
Private sector employers	100	loss
All employees	300	loss
Self-employed	400	loss
PSBR	900	loss
TOTAL BURDEN	1700	

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NIC Changes

OPTION 1: REPLACE SERPS WITH 3 YEAR PHASED MINIMUM PENSION REQUIREMENT
2% in 1987/8; 3% in 1988/9; 4% in 1989/90 £bn.

(£bn)	1987-8	1988-9	1989-90
Effects on private sector employers' costs			
Extra NICs	-0.2	-0.4	-0.8
Contributions to private schemes	+0.35	+0.6	+0.8
Gross increase in employers' costs	+0.15	+0.2	0
Less tax relief	0	0	-0.1
Net increase in employers' costs	+0.15	+0.2	-0.1
Effects on private and public employees			
Extra NICs	-0.1	-0.2	-0.4
Contributions to private schemes	+0.4	+0.6	+0.9
Gross increase	+0.3	+0.4	+0.5
Less tax relief	-0.1	-0.15	-0.2
Net increase (ie reduction in take-home pay)	+0.2	+0.25	+0.3
Effect on self-employed			
Extra NICs	+0.1	+0.3	+0.5
Less tax relief	0	0	-0.1
Net increase	+0.1	+0.3	+0.4

16½ Phased NIC

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OPTION 1: REPLACE SERPS WITH 3 YEAR PHASED MINIMUM PENSION REQUIREMENT
2% in 1987/8; 3% in 1988/9; 4% in 1989/90

A: OVERALL IMPACT

(£bn)	1987/8	1988/9	1989/90
Public Expenditure			
- savings agreed by MISC III	-0.3	-0.5	-0.5
- higher public sector employers' NICs	+0.2	+0.3	+0.4
- higher public sector pension contributions	+0.1	+0.1	+0.1
Total public expenditure	NIL	-0.1	NIL
Revenue			
- lower rate rebates	+0.5	+0.5	+0.5
- tax relief on contributions	-0.1	-0.15	-0.2
- NICs: private sector	-0.2	-0.3	-0.7
public sector	+0.2	+0.3	+0.4
- higher public sector pension contributions	+0.1	+0.1	+0.1
Total Revenue	+0.5	+0.45	+0.1
Total PSBR	-0.5	-0.55	-0.1

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16½% phase
NIC

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OPTION 1: REPLACE SERPS WITH MINIMUM PENSION REQUIREMENT IN APRIL 1987

1987/8 (£bn)	Contracted out	Contracted in	Total
Effects on private sector employers costs			
Extra NICs	+0.2	-0.4	-0.2
Contributions to private schemes	0	+0.35	+0.35
Gross increase in employers costs	+0.2	-0.05	+0.15
Less tax relief	0	0	0
Net increase in employers costs	+0.2	-0.05	+0.15
% of Low Cost			
Effects on private and public employees	+0.2	-0.3	-0.1
Extra NICs	0	+0.4	+0.4
Contributions to private schemes			
Gross increase	+0.2	+0.1	+0.3
Less tax relief	0	-0.1	-0.1
Net increase (ie reduction in take-home pay)	+0.2	0	+0.2.

16½% phase
NIC

SECRET

OPTION 1: REPLACE SERPS WITH MINIMUM PENSION REQUIREMENT IN APRIL 1987

1988/9 (£bn)	Contracted out	Contracted in	Total
Effects on private sector employers costs			
Extra NICs	+0.4	−0.8	−0.4
Contributions to private schemes	0	+0.6	+0.6
Gross increase in employers costs	+0.4	−0.2	+0.2
Less tax relief	0	0	0
Net increase in employers costs	+0.4	−0.2	+0.4
% of labour costs			
Effects on private and public employees			
Extra NICs	+0.3	−0.5	−0.2
Contributions to private schemes	0	+0.6	+0.6
Gross increase	+0.3	+0.1	+0.4
Less tax relief	0	−0.15	−0.15
Net increase (ie reduction in take-home pay)	+0.3	−0.05	+0.25

16½07 phase
NIC

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OPTION 1: REPLACE SERPS WITH MINIMUM PENSION REQUIREMENT IN APRIL 1987

1989/90(£bn)	Contracted out	Contracted in	Total
Effects on private sector employers costs			
Extra NICs	+0.7	-1.5	-0.8
Contributions to private schemes	0	+0.8	+0.8
Gross increase in employers costs	+0.7	-0.7	0
Less tax relief	+0.1	0	+0.1
Net increase in employers costs	+0.8	-0.7	+0.1
% of labour costs			
Effects on private and public employees			
Extra NICs	+0.5	-0.9	-0.4
Contributions to private schemes	0	+0.9	+0.9
Gross increase	+0.5	0	+0.5
Less tax relief	0	-0.2	-0.2
Net increase (ie reduction in take-home pay)	+0.5	-0.2	+0.3

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2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

My ref:

Your ref:

26 April 1985

Dear Mr Fowler

REVIEW OF SOCIAL SECURITY

The postponement of the Cabinet discussion of the social security review gives me time to raise with you two issues which were not properly discussed in MISC 111 and on which I find it difficult to accept your proposals.

The proposal to restrict the payment of Supplementary Benefit (SB) towards the cost of mortgage interest was first raised at the third meeting of MISC 111, but was not subsequently discussed. The suggestion then was that assistance might be recovered when the house of the recipient was sold on his death. There are obvious objections to this, and I can understand why you did not pursue it. It was superseded by the proposal for a 6-month waiting period which first came before MISC 111 when you presented your conclusions to the seventh meeting.

In my view this proposal would weaken our drive to make home ownership available to a wider section of the community. The present arrangements are a reassurance to tenants thinking of becoming owners for the first time. To restrict SB as you propose would reduce the number of tenants willing to take the risk. This would not reduce the size of the public sector. Nor would it offer significant savings, since the tenants deterred from owner occupation would continue to be eligible for help with their housing needs.

If the proposal goes ahead the building societies will complain bitterly about being expected to shoulder social housing responsibilities. If insurance were available to cover the mortgage payments no longer met by SB, that would help. However, insurance will not necessarily be available to those most at risk.

My second point is that the proposal to include help with water charges within the basic rate, at a notional average level, instead of paying actual charges as now, would cause severe problems. It would complicate the collection of charges, and increase hardship, particularly in high charge areas. It would also make it presentationally more difficult to raise charges in future because we should no longer be able to say that the poorest families are fully protected. Some families on SB could lose up to £1 a week (on the assumption that a notional figure of £1.14 is included in SB to take account of water charges).

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I believe we should consider both these proposals further before publishing them in the Green Paper. I should be very willing to discuss them with you before Cabinet takes the social security review as a whole.

I am sending copies of this to the Prime Minister, other members of the Cabinet, the Chief Whip, the Paymaster General and Sir Robert Armstrong.

Yours sincerely

S Wanderson

for

PATRICK JENKIN

Agreed by the Secretary of State and signed in his absence

The Rt Hon Norman Fowler MP

26 APR 1985

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From The Secretary of State for Wales

THE RT HON NICHOLAS EDWARDS MP

SECRET

8th May 1985

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Dear Norman

Thank you for sending me a copy of your letter of 1 May 1985 to Patrick Jenkin in reply to his letter of 26 April. The issues raised are of concern to me and I should like to comment on each of them.

I note what you say on the question of mortgage interest but however small the effect may be both in terms of the individuals concerned and our policies on the extension of home ownership and housing mobility, we would do well not to underestimate the political implications of what is proposed.

Water charges are high in Wales - the third highest in the league table. The cost of water in Wales is also a highly charged political issue and your proposal to increase the extent to which those ratepayers in receipt of supplementary benefit have to meet the charges will not be helpful. While I accept that there has been a policy of pushing up water charges, the fact remains that the main component is the cost of supply and that the primary factors affecting the cost of supply are topography and population density. Your proposal will affect particularly people in rural areas; the two areas above Wales in the league table being East Anglia and South West England.

Both District Councils and Water Authorities will face problems of collecting the additional costs faced by ratepayers. The Welsh Water Authority already has the highest record of default in the country. The effect of the changes you propose would undoubtedly worsen the debt problem.

Finally, I turn to arrangements for reimbursing local authorities for housing benefit expenditure. I agree that at the time of changeover we should continue the same level of central government payments to local authorities. We must recognise, however, that if the element of expenditure to be subsumed within the RSG arrangements is not met by a real increase in the level of resources made available for relevant expenditure and grant, local government will regard it as a totally unjustified additional burden. This will be particularly so in the case of the County Councils who would suffer even though the changes relate only to District Council activities.

Yours ever

Nick

Rt Hon Norman Fowler MP
Department of Health and Social Security
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SE1 6BY

Copies of this letter go to the Prime Minister, other members of the Cabinet, the Chief Whip, the Paymaster General and Sir Robert Armstrong.

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