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cc MASTER SET

10 DOWNING STREET

From the Private Secretary

6 May 1985

Dear Steve,

SOCIAL SECURITY REVIEWS: PENSIONS

The Prime Minister held a meeting this evening to discuss the future of pension provision. Present were your Secretary of State, the Lord President, the Chancellor of the Exchequer, the Secretary of State for Trade and Industry, the Chief Secretary, the Chief Whip, the Minister of State HM Treasury, and the Minister for Social Services. Also present were Mr. Brearley, Mr. Redwood and Mr. Willetts. The meeting had before it your Secretary of State's minute of 6 May; the note by officials attached to your letter to me, also of 6 May; and a note by the Chief Economic Adviser to the Treasury on the economic implications of increasing pension fund income. The Prime Minister expressed her appreciation for the substantial work which officials had put in to the preparation of these papers over the weekend.

The Secretary of State for Social Services said the latest proposal sought to take account of the Chancellor's concerns, both for the public sector accounts and for the impact on other sectors of the switch from a pay-as-you-go SERPS to funded private provision. It also sought to meet the difficulties for those nearing retirement which had been identified at the previous meeting. There had been general agreement that the liabilities of SERPS could not be allowed to carry on accumulating. The choice was either abolition and replacement with alternative provision; or a modified SERPS. The political difficulty of cutting back the benefits under a modified SERPS should not be underestimated. He therefore felt that the way forward was a scheme along the lines proposed in the Cabinet paper but with extended transitional provisions to soften the immediate impact. A further merit of compulsory private provision was that it would encourage the development of personal pensions which could not co-exist with SERPS.

The Chancellor agreed that the scheme now proposed went a substantial way to meet the concerns he had expressed. The short-term costs to the PSBR would be manageable but he hoped that in the discussions leading up to legislation nothing would be conceded which added to those costs. He also urged that the Government should not give way to pressure from large-scale business with contracted out schemes. The note by officials showed that the costs to such companies were only a fraction of those which the CBI had publicised a few days earlier. The Chancellor did, however, express concern about the impact on transferability and on compliance costs for small businesses. The Secretary of State said that the proposals had to be seen against the background of the measures now being enacted to encourage transferability and give a better deal to early leavers. The legislation on personal pensions would provide a simple way for small employers to contribute to the pensions of their employees.

In discussion it was noted that there was a sharp discontinuity between the pension which would be received by an employee now aged 52 who would remain with SERPS until retirement and that received by someone aged 51 who would contribute for fifteen years to a funded scheme. It was agreed that some disadvantage was the inevitable consequence of moving from a scheme that was over generous to one that was based on realistic assumptions of what could be afforded. In practice many people would contribute more than a minimum 4 per cent or would stay at work slightly longer. Nevertheless, it was agreed that ways should be investigated of smoothing the discontinuity, e.g. by adding a bonus to the SERPS pension of those just below the cut-off.

In further discussion, the Chancellor queried whether public sector employees in unfunded schemes should be allowed to take personal pensions. This could have an adverse effect on the PSBR. Although doubts were expressed about how many public servants would take this option, it was agreed that he should discuss it further with the Secretary of State for Social Services.

Summing up this part of the discussion, the Prime Minister said the meeting agreed that the scheme now before it should be put to Thursday's Cabinet meeting. She invited the Secretary of State for Social Services to circulate a paper to Cabinet setting out its main features.

The Secretary of State for Social Services said he had originally hoped to issue the Green Paper on 22 May. He wished, however, to consider the merits of waiting until Monday 3 June, immediately after the Whitsun Recess. The earlier date would put an end to uncertainty but, with Parliament in recess, it would be more difficult to follow up the initial presentation. Conversely the later date would allow more time to prepare the presentation and would allow the initial statement to be followed up in the House, though at the expense of extending the period of uncertainty. It was agreed that he would consider the pros and cons with the business managers.

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I am copying this letter to Janet Lewis-Jones (Lord President's Office), Rachel Lomax (HM Treasury), John Mogg (Department of Trade and Industry), Richard Broadbent (Chief Secretary's Office), Murdo Maclean (Chief Whip's Office), Mike Norgrove (Minister of State's Office, HM Treasury), Colin Phillips (Office of the Minister for Social Security) and Mr. Brearley.

Yours sincerely

Andrew Turnbull

(ANDREW TURNBULL)

Steve Godber, Esq.,
Department of Health and Social Security.