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SECRET

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PRIME MINISTER

Review of Social Security: Final Decisions

FLAG B —— (C(85)27)

BACKGROUND

The Cabinet last considered the Social Security Review at their meetings on 2 and 9 May 1985 (CC(85)15th Conclusions and CC(85)16th Conclusions) when they approved the Review package broadly as it went on to be published in the Green Paper. Following the consultations on the Green Paper, the Social Services Secretary returned to MISC 111 seeking modifications in the previously agreed proposals. Modifications were agreed at MISC 111(85)8th, 9th and 10th Meetings, and the Social Services Secretary now seeks Cabinet ratification of those decisions, so that the White Paper can be published before Christmas. The Social Security Bill would then be introduced after Christmas, with Second Reading in the second half of January. Mr Fowler then envisages Royal Assent by the end of July, but that is extremely optimistic: Royal Assent after the summer recess is much more realistic.

2. The main changes from the Green Paper package agreed by Cabinet in May are as follows.

(a) Pensions

3. Cabinet agreed to the abolition of the State Earnings-Related Pensions Scheme (SERPS), with appropriate transitional protection, and its replacement by a system requiring minimum private pension arrangements. MISC 111 have now agreed to modification rather than abolition of SERPS, on the basis that modification will still deliver large savings (now estimated at over £12 billion by 2033 at November 1985 prices). The main modifications are to base pensions under SERPS on 20 per cent of average life-time earnings (instead of the existing 25 per cent of the best 20 years' earnings) and to reduce the proportion of a pension

the figure was earlier £10.3bn.

inherited by the surviving spouse to 50 per cent from the existing 100 per cent. These reductions in cost make it possible to transfer to approved schemes the responsibility for inflation-proofing contracted-out pensions up to 3 per cent a year, without incurring the adverse PSBR effects of increasing the contracted-out rebate. MISC 111 also agreed that the reductions in SERPS should be balanced by various measures to make occupational schemes and personal pensions more attractive. In particular, there should be a new universal right for employees to opt for personal pensions, and there should be a special 2 per cent bonus on the contracted-out rebate for 5 years for new occupational schemes and personal pension holders. Annex A to the Social Services Secretary's paper sets out the pensions issues fairly and clearly.

(b) Income-Related Benefits

4. Cabinet agreed to

(i) the replacement of supplementary benefit with a new simplified system of income support backed by a discretionary social fund.

(ii) radical simplification of and reduction in housing benefit and in particular a ceiling on the amount of housing benefit payable in respect of domestic rates so that everyone paid 20 per cent of their rates

(iii) replacement of Family Income Supplement with an improved Family Credit Scheme to be paid through the wage packet.

(iv) miscellaneous reforms in maternity allowance and widows' benefit, and replacement of maternity grant and death grant with discretionary selective provision through the social fund.

5. The Secretary of State for Social Services has proposed no change in the structure of this package but MISC 111 have agreed a number of

changes, some of which are set out in Annex B of the Social Services Secretary's paper. Those listed in Annex B comprise more generous treatment under income support than was originally proposed for couples under 25; reduced - rather than nil - assistance towards mortgage interest during the first 6 months on income support; reversion to separate housing benefit tapers for rent and rates; and the retention of local housing benefit schemes for war pensioners. More substantially, however, MISC 111 also agreed (although this is not referred to in the present paper) that the Social Services Secretary might discuss with the Chancellor of the Exchequer how he might accommodate increases he wanted to make to the proposed pensioner premium under income support to reduce the number of pensioner losers, and to the family credit arrangements to improve incentives. The Social Services Secretary felt that these concessions were politically necessary for the passage of the Bill, but you were clear in MISC 111 that the overall social security programme must be contained within the figure for 1988-89 that had been published as a provisional one in the Autumn Statement. The Chancellor of the Exchequer and the Social Services Secretary have now agreed how the cost of the concessions that Mr Fowler wants to make can be offset within the Autumn Statement figure, which is now final. Accordingly, the tables of gainers and losers circulated to the Cabinet separately by Mr Fowler take account of these changes. (The Social Services Flag C Secretary's minute to you of 25 November sets out the details of how the additional expenditure in 1988-89 can be offset.)

(c) Timing of Changes — Apl 1988

6. The Cabinet agreed to introduction of the changes in April 1987. MISC 111 subsequently agreed to defer implementation of the main changes until April 1988 to accommodate slippage in the timetable for introduction of the Social Security Bill as a result of the pensions changes and to allow local authorities and businesses a larger time-scale to prepare for implementation. The Social Services Secretary, however, agreed in both MISC 120 and MISC 111 to advance implementation of certain measures to secure savings in earlier years and these are reflected in the public expenditure totals agreed by Cabinet and published in the Autumn Statement.

MAIN ISSUES

7. This Cabinet consideration is the final stage of policy clearance for proposals that have been exhaustively discussed already, and there are no substantial issues that do not emerge from the background summarised above. So far as pensions are concerned, what is at issue is the change of course towards a less radical approach to SERPS that was explicitly rejected in the Green Paper. The adjustments to the earlier proposals on the structure of income-related benefits are relatively small - the basic structure remains unaltered - but Cabinet will no doubt wish to take a final political view of the distribution of gainers and losers. This is illustrated in the Tables attached to Mr Fowler's separate note of 26 November. Tables 1 and 2 show the effects the changes would have if the new structure were substituted for the existing structure as it is in November 1985. Tables 3 and 4 show the effects in cash terms, taking into account (as the Chief Secretary recommended at MISC 111) the mitigating effects on the pattern of gainers and losers of uprating of benefits and the agreed transitional protection arrangements. Tables 1 and 3 also exclude the effects of the proposed minimum 20 per cent rates contribution proposal, thereby substantially reducing the number of losers.

8. I suggest that in any discussion of the distributional effects you concentrate on Tables 2 and 4, which include the 20 per cent rate contribution, and are therefore on the same basis as considered by MISC 111 (subject to some changes in the numbers as a result of Mr Fowler's latest agreement on savings with the Chancellor of the Exchequer). However, since it is not possible at this stage to quantify the effects of the interaction between the 20 per cent rule and the rates reform proposals (final decisions on which will not be taken until well into next year) there is some justification for showing also the distributional effects (as in Tables 1 and 3) excluding the former. But great care will need to be taken in presenting this in order to avoid the charge of being deliberately disingenuous and misleading.

9. There are also the following subsidiary points.

(a) You asked the Social Services Secretary at the MISC 111 meeting on 31 October to consider whether the right to a personal pension might be implemented in 1987, before the main pension s measures. We understand that Mr Fowler is about to write to say that this would be undesirable for a number of reasons, and especially because the investor protection provisions of the Financial Services Bill must be in position before the right to a personal pension is given effect. (If the right were implemented before the investor protection machinery was in place, insurance companies would have an effective monoply of the new business in personal pensions).

(b) You have been concerned in MISC 111 that in public service pension schemes the right to a personal pension should be a meaningful one, while safeguarding the PSBR against large movements to fully funded arrangements. I understand that the Chancellor of the Exchequer and the Social Services Secretary hope to agree later today with the Ministers concerned that the White Paper should take the line that public service employers should not recognise liabilities to make payments above the contracted out rebate unless the employee is himself making additional contributions directly to his pension.

They have done so, and the Chancellor is writing.

(c) The Northern Ireland Secretary has recorded that the rationale of the 20 per cent contribution to rates does not apply clearly in Northern Ireland, where the range of local authority services is limited, and he himself sets the rate. That is perfectly true in itself, but Mr King does not appear to be going so far as to argue for any change in the longstanding arrangement for parity throughout the United Kingdom on social security. This point can be best taken as advance warning of a presentational issue.

HANDLING

10. You may wish to ask the Social Services Secretary to introduce his paper in two parts - pensions first, and then all other matters.

11. On each part, you may wish to ask the Chancellor of the Exchequer to speak next, and then to invite Ministers who are not members of MISC 111 to express their views.

12. On the next steps, you will wish to remind the Cabinet that publishing the White Paper in mid-December depends on the text being finanised next week. If colleagues have any drafting points on the text Mr Fowler is circulating separately to the Cabinet (hopefully later today), you will hope that they can settle them direct with him before 4 December. The Bill must have its Second Reading by the end of January, and you may wish to stress that this must not slip.

Your copy is below.

13. On presentation of the White Paper you will wish to invite Mr Fowler to consult the Lord President and the Chancellor of the Duchy of Lancaster. So far as the local government finance Green Paper is relevant, the Secretary of State for the Environment should also be involved.

And the Chancellor of the Exchequer

CONCLUSIONS

14. You will wish

(i) to ensure that Cabinet agree to any significant changes from the proposals made in the Green Paper;

(b) to secure the agreement of Cabinet to the revised proposals being published as a White Paper in mid-December;

(c) to invite Cabinet members to take up any points they may have on the text of the White Paper with the Social Services Secretary so that they can be settled before 4 December;

(d) to invite the Social Services Secretary to discuss presentation of the White Paper with the Lord President, the Chancellor of the Duchy of Lancaster and (so far as local government finance studies are relevant) with the Secretary of State for the Environment.

RA

27 November 1985

10 DOWNING STREET

Prime Minister

RTA invites a discussion of gainers and losers. There has to be recognition of this, but discussion risks contention to no great purpose.

The important point is that the presentation of the figures and generally should be agreed between

Mr Fowler

Lord Whitelaw

Mr Tebbit

Chancellor

and Mr Baker for rates.

DRN

MT, 27/11