

CONFIDENTIAL



10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

20 November 1989

Dear Helen,

NATIONAL INSURANCE FUND

The Prime Minister has seen your Secretary of State's letter of 14 November to the Lord President. The Prime Minister would like to discuss with colleagues the proposed abolition of the allocation from the Fund to the Health Service. We are hoping to arrange a meeting of E(A) for later this week when this issue can be placed on the agenda.

I am copying this letter to Private Secretaries to members of E(A), H Committee and to Sir Robin Butler.

*Yan,
Pat*

PAUL GRAY

Ms. Helen Dudley,
Department of Social Security

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MG

TR 9764p

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DEPARTMENT OF SOCIAL SECURITY

Richmond House, 79 Whitehall, London SW1A 2NS

Telephone 01-210 3000

From the Secretary of State for Social Security

CCP4

Paul Gray Esq
Private Secretary
to the Prime Minister
10 Downing Street
LONDON SW1

16 November 1989

Jean Paul ~~Paul~~ RA

NATIONAL INSURANCE FUND

I have been asked by Cabinet Office to ensure that members of E(A) receive a copy of a letter my Secretary of State has sent to the Lord President, copied to members of H Committee, on the National Insurance Fund, dated 14 November. This is attached, and I am copying it to private secretaries to members of E(A).

Yours

Helen

HELEN DUDLEY
Private Secretary

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Arbhr

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PRIVY COUNCIL OFFICE

WHITEHALL, LONDON SW1A 2AT

16 November 1989.

Dear Stuart,

will obtain if
required

The Lord President has seen your Secretary of State's letter of 14 November about the National Insurance Fund.

He can see why the conclusions set out in the letter were reached and agrees that there might indeed be scope for presenting such a change very positively. However, he considers that such a major policy change deserves collective discussion to ensure that all the potential difficulties have been identified. This could most appropriately take place in E(A) where such matters have been discussed in the past.

I am copying this letter to the Private Secretaries of members of H and E(A) Committees.

Yours sincerely,

Gillian Baxendine

GILLIAN BAXENDINE
Private Secretary

Stuart Lord Esq
PS/Secretary of State for Social Security



10 DOWNING STREET

Prime Minister

You were not able to
finish the attached last
night. Content with the
proposed change?

RCG

17/11

I would rather speak to
them about it. It is
a shifty device.

ms

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DEPARTMENT OF SOCIAL SECURITY

Richmond House, 79 Whitehall, London SW1A 2NS

Telephone 01-210 3000

From the Secretary of State for Social Security

Prime Minister

The Rt Hon Sir Geoffrey Howe QC
Lord President of the Council
Privy Council Office
Whitehall
LONDON
SW1A 2AT

This proposes ending all links between the NI Fund and the NHS - a principle to which you have attached importance in the past. My own view is that the ~~present~~ present arrangements are artificial, and there is a good case for the change proposed - see the points at X on the next page. But are you content to let the proposal go ahead.

14 NOV 1989

Geoffrey

NATIONAL INSURANCE FUND

PRC 6

16/11

I am writing to let you know the outcome of recent discussions I have had with John Major and Kenneth Clarke about the future management of the National Insurance Fund; and to seek colleagues agreement to the action I propose to take. This will involve legislation in my 1989-90 Bill so as to abolish from April 1991 the current practice whereby a proportion of the Fund's income is used to finance the Health Service.

Despite this year's Budget reductions in the amount of national insurance paid by employees, the balance in the Fund will remain well above the Government Actuary's recommended minimum level until the end of 1990-91. But this situation will change significantly as the costs of our personal pension initiative begin to be felt. On the basis of current economic assumptions, the Actuary has forecast that the balance will fall below his minimum recommended level in 1991/92; and that, by the following year, the Fund is likely to go into deficit and remain there well into the mid 1990s.

The take up of personal pensions has been much higher than we expected. Already over 3 million applications have been approved and this figure is likely to go as high as 5 million within the next two years. The success of the initiative is much to be welcomed because it means that a large proportion of the working population are now taking responsibility for their own pension arrangements by choosing not to rely on the state earnings related scheme. Eventually, this will produce benefit savings but, in the short term, the costs of rebates and incentives associated with our initiative will push the Fund into deficit unless remedial action is taken.

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The prospect of having to meet these costs with sharp increases in national insurance contributions is plainly unattractive. I therefore proposed to the Chancellor that we could overcome our difficulties with a package of measures, the main element of which was a set of borrowing powers for the Fund. These powers would have removed the obligation to maintain the Fund at a certain percentage of benefit expenditure while the other measures were designed to ensure that the Fund did not fall below zero. However, John Major felt strongly that borrowing powers could be portrayed as a relaxation of financial prudence and might cast doubt on our overall fiscal stance.

The Chancellor and I have therefore concentrated our attention on the allocation made each year from the Fund to the Health Service. This currently stands at over £4 billion and is calculated as a percentage of the contributions paid by employees, employers and the self-employed. By using powers already available to vary the percentage by a small amount each year, we have allowed the allocations to rise steadily since we took office. This has enabled us to prevent the Fund from reaching too high a surplus. The allocation does not, of course, affect Government decisions on the overall level of public expenditure on the NHS; it is purely a technical funding device.

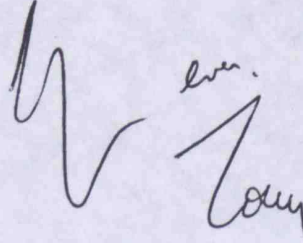
The existing powers do not permit us to reduce the allocation by a sufficient amount to rescue the NI Fund. We have considered the possibility of legislating to set the allocation at zero until the Fund's problems are overcome but Kenneth Clarke has expressed grave reservations about the presentational problems this would pose. It would mean, in effect, that although we still believed in the principle of partly financing the Health Service from national insurance contributions we were unwilling to support that principle in practice for reasons of short-term expediency. This would maximise the opportunity for the Opposition to claim that we had mis-managed the Fund - even perhaps to argue that the NHS was to suffer because of subsidies for private pension provision. Both John Major and I accept that this approach must be ruled out because of the presentational difficulties.

Our proposal, supported by Kenneth Clarke, is to abolish the allocation altogether leaving a situation in which the health Service is visibly seen to be funded only from taxation, and from receipts from charges and income generating activity. There are of course many people who believe that the whole, or a large part, of their NI contribution goes to the NHS and influences expenditure on it. We shall need to correct that. Indeed, I believe we can present the change very positively, emphasising that access to the NHS does not depend upon an individual having paid contributions. The abolition of the allocation is entirely logical and follows naturally on last year's decision to end the Treasury Supplement.

The abolition of the NHS allocation will resolve the problems facing the Fund and ensure that the balance remains above the Actuary's recommended minimum for the next five years at least. It will mean that no other action will be necessary and will enable us to

maintain our record of no increases in contributions for employers and employees since 1983/84. I hope colleagues will agree that this represents the best possible solution.

I am copying this minute to other members of H Committee and Sir Robin Butler.

A handwritten signature in dark ink, appearing to read 'Tony Newton', with a stylized flourish above it.

TONY NEWTON

ECON POL: Budgetary pr 10