



Treasury Chambers, Parliament Street, SW1P 3AG
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PRIME MINISTER

E(A), THURSDAY 23 NOVEMBER: NATIONAL INSURANCE FUND

We are to discuss at E(A) on Thursday Tony Newton's proposal for dealing with the projected deficiency in the national insurance fund. As Tony's letter of 14 November to Geoffrey Howe makes clear, he has agreed his approach with Kenneth Clarke and me. But I thought it would be helpful if, in advance of the meeting, I set out briefly the reasons why I support Tony's proposal.

The Government Actuary estimates that the balance in the national insurance fund will fall below the prudential minimum (equivalent to 17 per cent of annual benefit expenditure from the fund) sometime in 1991-92. The balance was already expected to fall substantially as a result of the reform of employees' NICs announced in the Budget and implemented last month. What has taken the projections below the prudential minimum is the reduction in income to the fund arising from the success of personal pensions. Nearly 3½ million people have so far taken out personal pensions (the great majority having opted out of SERPS), far more than anyone expected. This is, of course, extremely welcome and will reduce expenditure on SERPS in the long term. But, in the short term, it is clear that we have to take action to maintain the balance in the fund.



In principle, there are several options available (all of which would require primary legislation):

- (a) increase national insurance contributions;
- (b) reinstate the Treasury Supplement, the taxpayers' subvention to the fund which was abolished in the 1989 Social Security Act;
- (c) allow the fund to borrow;
- (d) abolish the NHS allocation.

An increase in NICs is obviously unattractive, particularly as the increase would take effect in April 1991, and reinstating the Supplement would be an embarrassing reversal. Tony and I have considered (c). As he says, I would be most unwilling to take the risk that allowing the fund to borrow would be portrayed as a relaxation of financial prudence and raise doubts about our overall fiscal stance.

This leaves the NHS allocation. At present, about 10 per cent of total NICs are used to help pay for the NHS, instead of national insurance benefits. As you know, from the point of view of public finances, this is purely an accounting device, which makes no difference to the level of expenditure on the NHS nor to the amount of money we raise through NICs. If we were to abolish it, the same level of expenditure on the health service would be financed entirely out of taxes (plus income from charges etc) rather than a mixture of taxes and NICs. NICs would be devoted entirely to financing national insurance benefits, and the Government Actuary estimates that the balance in the fund would remain comfortably above the prudential minimum.

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The Opposition may try to argue that ending the allocation would reduce resources available for health. But this would be an entirely bogus argument, and I doubt whether they could make much of it. The allocation is worth £4 billion, and it would not be credible to contend that we were reducing the health programme by such a large amount, especially as we have just announced a significant increase in planned expenditure over the Survey period.

So while ending the allocation will need careful explanation (and a robust dismissal of any Opposition mischief - making) I think it is the best solution to the problem we must tackle.

I am copying this minute to the other members of E(A).

A handwritten signature in blue ink, appearing to read 'John H.' with a stylized flourish.

JOHN MAJOR
22 November 1989

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