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Chas Lawson

PART C

SECRET

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PART C

1985 PUBLIC EXPENDITURE SURVEY (PES): PARTICULAR PROGRAMMES

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PART C

DD: 25 years

[signature] 5/9/95

Begins: ~~8/5/85~~ 15/3/85

Ends: ~~16/9/85~~ 4/6/85 (CONTINUED)

FROM: MISS M E PEIRSON
DATE: 15 March 1985

1. MR CASSELL

2. CHANCELLOR OF THE EXCHEQUER

Copy attached for:

Mr Turnbull - No 10

cc List A	List B (distributed at 2.30 pm, 18 March)	
Sir P Middleton	Chief Secretary	Mr Peretz
Sir T Burns	Financial Secretary	Mr Mowl
Mr H Evans	Economic Secretary	Mr Stibbard
Mr Battishill	Minister of State	Mr M Williams
Mr Lankester	Mr Bailey	Mr Powell
Mr Collinson	Mr Odling-Smee	Mr Cropper
Mr Devereux	Mr Scholar	Mr Wells - CSO
Dr Webb	Mr Burgner	Mr Walton - IR
	Mr Folger	Mr Wilmott - C & E

MONTHLY NOTE ON THE PSBR

1. I attach a report on the PSBR outturn for February. This outturn will be published by press notice at 2.30 pm on Monday 18 March, the day before the Budget (when a forecast for 1984-85 as a whole will be published).

2. In this note, as usual, outturn in the latest month (February) is compared with the forecast made a month ago. Outturn in the first 11 months of 1984-85 (April-February) is compared with the 1984 Budget profile for those months, and also with the outturn for the same period in 1983-84. Forecasts for March are included. The press notice is confined to comparisons between outturn in 1984-85 with outturn in 1983-84.

MEP

MISS M E PEIRSON

PUBLIC SECTOR BORROWING

Summary

- The PSBR for February is provisionally estimated as a net repayment of debt of £0.2 billion, compared with last month's forecast of net borrowing of £0.4 billion. Central government's own account recorded a surplus of £0.6 billion, compared with forecast borrowing of £0.2 billion. Local authorities borrowed £0.4 billion, and public corporations showed a very small surplus.

- Borrowing in the first eleven months of 1984–85 (£7.6 billion) was about £2.3 billion higher than the Budget profile. In April–February last year the PSBR was £7.5 billion.

- The PSBR for 1984–85 is now expected to be around £10½ billion, although there are still very large uncertainties. This forecast implies borrowing of £2.9 billion in March. This is about £¾ billion higher than in March 1984 and close to the outturn for March 1983. The March surge in Supply Expenditure is expected to be greater than last year.

Figures in this report are not seasonally adjusted and also may not sum precisely because of rounding.

Chart 1 : Comparisons with Budget profiles for 1984-85

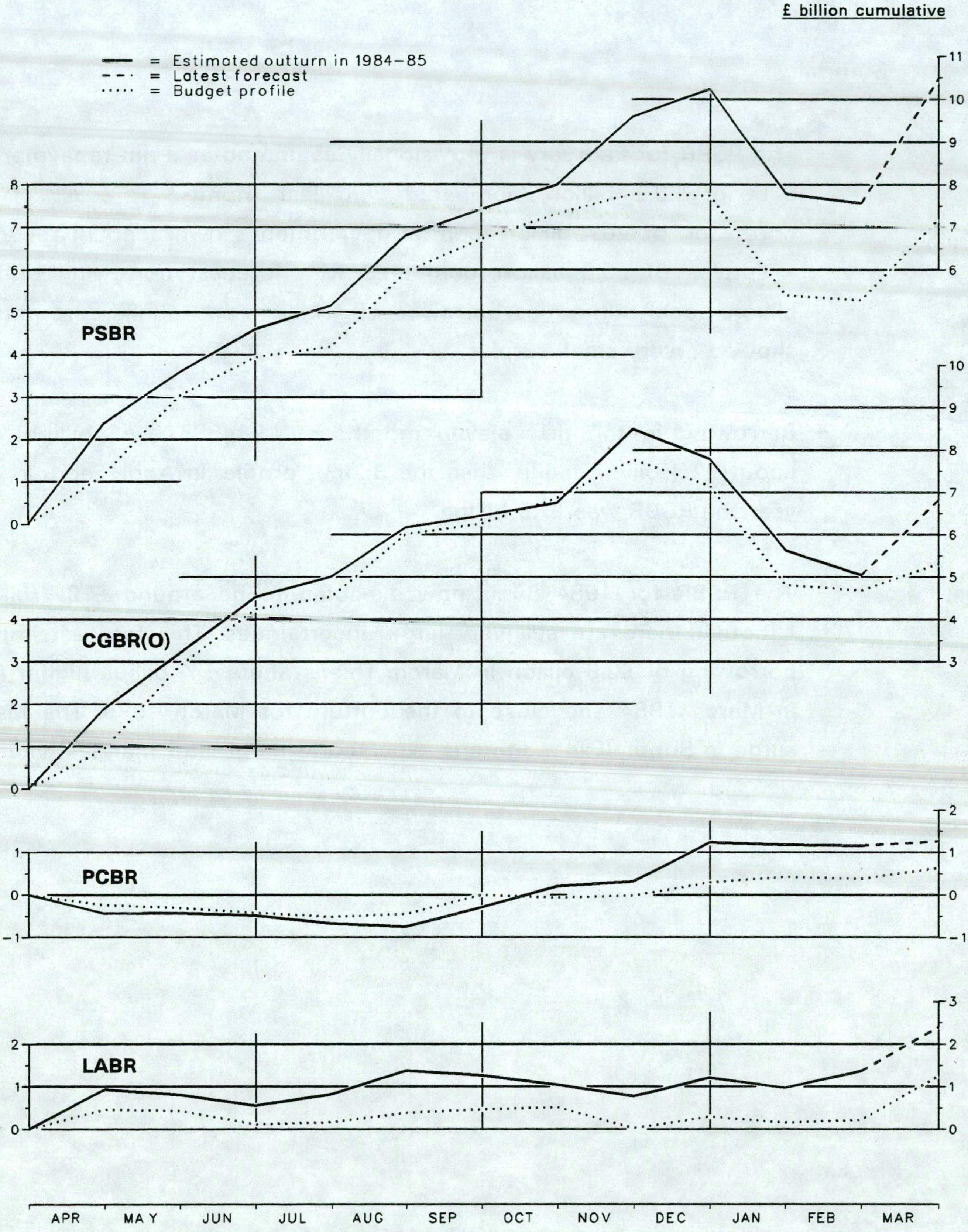
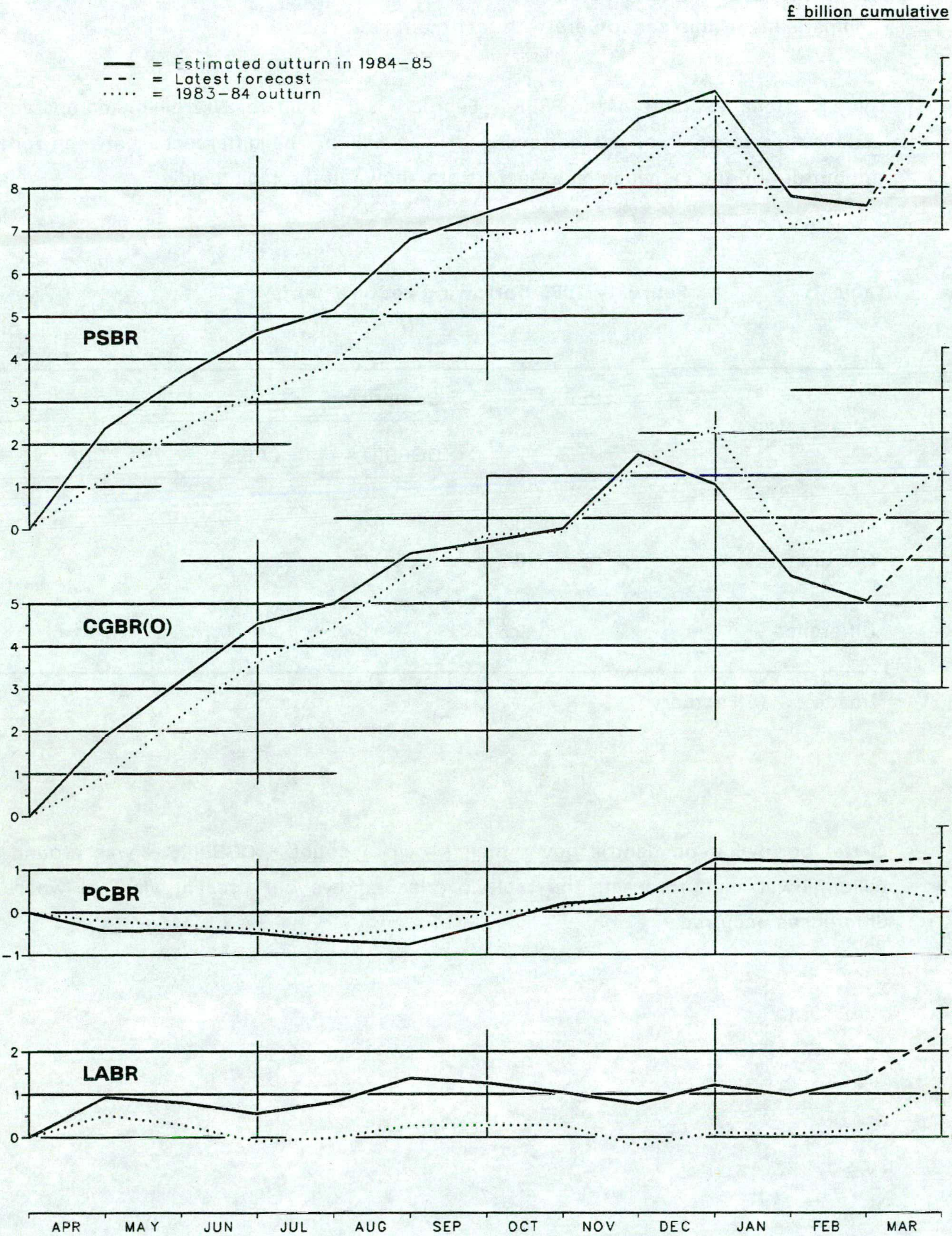


Chart 2 : Comparisons with last year's outturns



<u>Borrowing in February</u>

(Comparisons in this section are with last month's forecast)

The provisional estimate of the PSBR in February is a surplus of £0.2 billion, compared with last month's forecast of net borrowing of £0.4 billion. The differences between forecast and outturn on the individual sub-sectors are shown in the table below.

Table 1: **February 1985 borrowing requirements**

£ billion

	PSBR	Comprising		
		CGBR(O)	LABR	PCBR
Forecast*	0.4	0.2	0.3	-0.1
Outturn	-0.2	-0.6	0.4	-
Difference	-0.6	-0.8	0.1	0.1

*made on 15 February

2. Net borrowing on <u>central government's own account</u> - CGBR(O) - was around £0.8 billion lower than forecast. The table overleaf shows our present view of where the differences occurred.

£ billion (-indicates lower borrowing)

Inland Revenue receipts	-0.3
Customs and Excise receipts	-0.3
Supply Expenditure	-0.4
National Insurance Fund	+0.2
Net effect on CGBR(O)	-0.8

3. Higher Inland Revenue receipts in February appear to be mainly due to the timing of both Income and Corporation tax receipts; shortfalls recorded in January appear to have been made up while some receipts due in March may have been paid early. Customs and Excise receipts were also substantially higher than forecast: this may be due to additional receipts resulting from the change in VAT on imports. Supply expenditure on a cheques issued basis was lower than forecast mainly due to the slippage of payments to defence contractors and the postponement of grant to the National Coal Board. A minor deficit was recorded on the National Insurance Fund in place of the forecast surplus.

4. Local authorities borrowed about £0.4 billion in February, about £0.1 billion more than forecast last month. This error is small compared with the recent erratic pattern of local authority borrowing. (The estimate for February is based on a smaller sample than usual because the GLC made no return.)

5. Public corporations showed a small surplus in February, which was about £0.1 billion smaller than the surplus forecast last month, mainly because of the postponement of grant to the National Coal Board (see paragraph 3).

April to February outturn

(Comparisons in this and following sections are with the Budget profile)

6. The cumulative PSBR for the first eleven months of 1984-85 was £7.6 billion. This is about £2.3 billion above the Budget profile (see Chart 1 and Table 2) and about £0.1 billion above the same period last year (Chart 2).

Table 2: **Total April-February borrowing requirements**

£ billion

	PSBR	Comprising		
		CGBR(O)	LABR	PCBR
Budget forecast	5.3	4.7	0.2	0.4
Outturn	7.6	5.0	1.4	1.2
Difference	2.3	0.4	1.1	0.8

7. Cumulative borrowing in April-February on central government's own account was £0.4 billion higher than the Budget profile. Reasons were lower Inland Revenue receipts (by £0.6 billion) and a smaller surplus on the National Insurance Fund (by £0.7 billion - see paragraphs 8 and 9.) These factors were partially offset by higher Customs and Excise receipts (by £0.4 billion - see paragraph 9), higher oil royalties (by £0.4 billion) and other changes. Supply expenditure, excluding on-lending, was £0.5 billion higher than in the Budget profile, more than acounted for by advance payments to the EC; however, this excess is offset by a reduction in payments to the EC from elsewhere in the account.

8. The Inland Revenue shortfall reflects lower receipts of Income and Corporation tax. The Income tax shortfall is due to: lower PAYE receipts because of the miners' strike; lower Schedule D from the self-employed (because of lower profits in 1983); and higher repayments (including those under MIRAS scheme which have been affected by higher interest rates). In addition mainstream Corporation tax receipts have been less than forecast in the Budget profile and a complete recovery before the end of the year seems unlikely. As a partial offset, PRT receipts are higher because of higher oil production and higher sterling oil prices (the main increase in PRT is however in March; it is known to have slightly exceeded earlier expectations). Also, duty on share transactions is higher because of higher share prices and turnover.

9. The Customs overshoot is mainly due to higher than expected receipts from the change in VAT on imports. The change is now estimated to have brought in £1.4 billion, compared

with the Budget forecast of £1.2 billion, owing to the lower value of sterling and high volume of imports. The reduction in the National Insurance Fund surplus results from a reduction in contributions (because of the miners' strike) and an increase in benefits (partly higher unemployment, partly increased take-up of invalidity benefit).

10. Local authorities borrowed about £1.4 billion in the period April-February, some £1.1 billion higher than the Budget profile. The difference reflects partly the likely capital overspend in the current year, and partly the high borrowing last April due to overspending last year.

11. Public corporations borrowed about £1.2 billion to end-February, compared with £0.4 billion in the Budget profile. Borrowing was below the Budget profile over the first half of 1984-85, but borrowing has been heavy over the last five months, reflecting the effects of the coal strike.

March

12. Table 5 shows the latest detailed profile of borrowing on central government's own account for March. The forecast is for net borrowing of about £1¾ billion, nearly £1¼ billion higher than the Budget profile.

13. Supply expenditure in March, excluding on-lending, is forecast to be higher by £1¼ billion than the Budget profile, mainly because of increased grants to the National Coal Board, and defence procurement postponed from earlier months. This forecast takes account of departments' F10 estimates of outturn, and does not imply any significant breach of cash limits. The forecast for March represents an increase of about 31 per cent on the average level of Supply in October - February, compared with corresponding increases of 27 per cent in March 1984, 36 per cent in March 1983 and 21 per cent in March 1982.

14. Apart from Supply, the 1984 EC refund expected in March 1985 in the Budget profile (and worth £½ billion) has now slipped into 1985-86. Debt interest payments in March are expected to be a little higher than in the Budget profile. These factors are partially offset by an increase in Inland Revenue receipts (by £¾ billion), mainly reflecting PRT (£1¾

billion, already received).

15. <u>Local authorities</u> are forecast to borrow just over £1 billion in March. This follows the pattern of the last 5 years, when the LABR has almost always been in the range £1.0 - 1.2 billion in March: the high borrowing occurs because in March no rate income is received and expenditure tends to be high. The CIPFA borrowing enquiries return also implies that March borrowing will be high.

16. <u>Public corporations</u> are expected to show net borrowing of around £0.1 billion in March. The Coal Board is expected to borrow £0.2 billion following the end of the stike, and the Electricity Supply Industry is expected to repay some of their borrowing out of their seasonally high receipts from customers.

17. Thus the PSBR in March is forecast at £2.9 billion, but there is a wide margin of error. (In March 1984 it was £2.3 billion and in March 1983 £2.9 billion).

<u>1984-85</u>

The February outturn seems broadly consistent with a forecast of £10½ billion for the year. There are still great uncertainties, however, about the March forecast.

Table 3: 1984-85: Outturns and latest forecasts

£ billion

	PSBR	Comprising		
		CGBR(O)	LABR	PCBR
1984-85				
Apr	2.4	1.9	0.9	-0.4
May	1.2	1.3	-0.1	-
Jun	1.0	1.3	-0.3	-0.1
Jul	0.6	0.5	0.3	-0.2
Aug	1.6	1.2	0.6	-0.1
Sep	0.6	0.3	-0.1	0.5
Oct	0.6	0.3	-0.2	0.5
Nov	1.6	1.7	-0.3	0.1
Dec	0.6	-0.7	0.4	0.9
Jan	-2.5	-2.2	-0.2	-
Feb	-0.2	-0.6	0.4	-
Mar	2.9	1.8	1.0	0.1
Cumulative				
Apr	2.4	1.9	0.9	-0.4
May	3.6	3.2	0.8	-0.4
Jun	4.6	4.5	0.6	-0.5
Jul	5.2	5.0	0.8	-0.7
Aug	6.8	6.2	1.4	-0.7
Sep	7.4	6.4	1.3	-0.3
Oct	8.0	6.8	1.0	0.2
Nov	9.6	8.5	0.8	0.3
Dec	10.2	7.8	1.2	1.2
Jan	7.8	5.6	1.0	1.2
Feb	7.6	5.0	1.4	1.2
Mar	10.5	6.8	2.4	1.3

Figures for April to February are outturns

Table 4: PSBR for 1984-85 - Comparisons with 1983-84 and Budget profile

£ billion

	1983-84	1984-85		Differences from	
	Outturn	Budget profile	Latest update[1]	1983-84 outturn	Budget profile
	1	2	3	3-1	3 2
Apr	1.2	1.2	**2.4**	1.1	1.2
May	1.1	1.9	**1.2**	0.1	-0.7
Jun	0.8	0.9	**1.0**	0.2	0.1
Q2	3.2	3.9	**4.6**	1.4	0.7
Jul	0.7	0.3	**0.6**	-0.2	0.3
Aug	1.7	1.8	**1.6**	-0.1	-0.1
Sep	1.2	0.8	**0.6**	-0.6	-0.2
Q3	3.7	2.8	**2.8**	-0.9	-
Oct	0.2	0.6	**0.6**	0.4	-
Nov	1.4	0.5	**1.6**	0.2	1.1
Dec	1.3	-	**0.6**	-0.7	0.7
Q4	2.9	1.0	**2.8**	-0.1	1.8
Jan	-2.7	-2.3	**-2.5**	0.2	-0.1
Feb	0.4	-0.1	**-0.2**	-0.6	-0.1
Mar	2.3	1.9	**2.9**	0.6	1.0
Q1	-0.1	-0.5	**0.2**	0.3	0.8
Cumulative					
Apr	1.2	1.2	**2.4**	1.1	1.2
May	2.4	3.0	**3.6**	1.2	0.6
Jun	3.2	3.9	**4.6**	1.4	0.7
Jul	3.9	4.2	**5.2**	1.3	1.0
Aug	5.6	6.0	**6.8**	1.2	0.9
Sep	6.9	6.7	**7.4**	0.6	0.7
Oct	7.1	7.3	**8.0**	0.9	0.7
Nov	8.5	7.8	**9.6**	1.1	1.8
Dec	9.8	7.7	**10.2**	0.5	2.5
Jan	7.1	5.4	**7.8**	0.7	2.4
Feb	7.5	5.3	**7.6**	0.1	2.3
Mar	9.7	7.2	**10.5**	0.7	3.3

[1]Figures for April to February are outturns

Table 5: Central government transactions – February outturn and latest forecasts for March

£ billion

	February		Latest forecasts
	forecast	outturn[1]	March
Receipts			
Consolidated Fund			
Inland Revenue	4.3	4.5	5.2
Customs and Excise	3.4	3.7	2.7
Other[2]	1.4	0.5	1.8
National Loans Fund			
Interest etc. receipts	0.4	0.4	0.8
Total Receipts	9.4	9.1	10.5
Expenditure			
Consolidated Fund			
Supply expenditure[3]	8.1	7.7	10.4
Adjustment to Supply Services basis[4]	–	-0.1	-0.5
Other	0.2	0.3	0.3
National Loans Fund			
Service of the national debt	1.0	1.0	1.0
Net lending	0.1	0.5	–
Total Expenditure	9.4	9.3	11.3
Other funds and accounts (+ increases borrowing) (– reduces borrowing)	0.4	-0.4	1.5
CGBR	**0.4**	**-0.2**	**2.4**
On-lending	0.1	0.4	0.6
CGBR(O)	**0.2**	**-0.6**	**1.8**

(1)Due to time lags in some items reaching their final accounting destination, figures of forecast and outturn may not be strictly comparable for the components identified, but there is no effect on the overall CGBR.
(2)Includes National Insurance Surcharge and receipts from sales of assets
(3)On a cheques issued basis. Supply includes an element of on-lending in the form of public dividend capital etc.
(4)Reflects changes in balances of departmental accounts with the Paymaster General, timing and other differences between cheques issued by departments and payments to them from the Consolidated Fund. An offset to this item is included in "Other funds and accounts".

Table 6: Central government transactions[1] – comparisons for 1983–84 and 1984–85

£ billion

	1983–84	1984–85	
	Outturn	Budget forecast	Latest update
Receipts			
Consolidated Fund			
Inland Revenue	45.9	50.5	50.5
Customs and Excise	31.4	35.0	35.3
Other[2]	11.0	12.6	12.6
National Loans Fund			
Interest etc. receipts	5.3	5.8	5.4
Total Receipts	93.7	103.9	103.9
Expenditure			
Consolidated Fund			
Supply expenditure[3]	86.7	91.7	93.8
Adjustment to Supply Services basis[4]	–	–	–
Other	4.3	5.0	4.5
National Loans Fund			
Service of the national debt	11.8	12.6	12.9
Net lending	3.4	4.9	2.4
Total Expenditure	106.2	114.2	113.6
Other funds and accounts (+ increases borrowing) (– reduces borrowing)	–0.2	0.8	0.4
CGBR	**12.3**	**11.1**	**10.1**
On-lending	4.1	5.8	3.3
CGBR(O)	**8.2**	**5.3**	**6.8**

(1)Due to differences in treatment of some items in the accounts between the periods/forecasts shown, and time lags in some items reaching their final accounting destination, figures for the components identified may not be strictly comparable.
(2)Includes National Insurance Surcharge and receipts from sales of assets.
(3)On a cheques issued basis. Supply includes an element of on-lending in the form of public dividend capital etc.
(4)Reflects changes in balances of departmental accounts with the Paymaster General, timing and other differences between cheques issued by departments and payments to them from the Consolidated Fund. An offset to this item is included in "Other funds and accounts".

PP

DEPARTMENT OF HEALTH AND SOCIAL SECURITY
Alexander Fleming House, Elephant & Castle, London SE1 6BY
Telephone 01-407 5522
From the Secretary of State for Social Services

John Selwyn-Gummer Esq MP
Paymaster General
Cabinet Office
70 Whitehall
LONDON
SW1A 2AS

16 March 1985

18/3

Dear John.

ENTERPRISE AND CAPITAL RULES

I am sorry that I have not replied before to your letter of 16 January about the treatment of capital in supplementary benefit. As you know, this issue is very much on the agenda as we consider together the outcome of the social security review.

I am personally sympathetic to the very clear feeling that has been expressed in the Party that the present capital rules are seen to penalise thrift and provide an incentive for people to run down their capital in order to claim benefit. It was also the view of the Supplementary Benefit Review led by Tony Newton that the present system creates an unsatisfactory cliff-edge of entitlement by debarring anyone with capital over £3,000. I do not think, therefore, there is anything in principle between us on the desirability of improving the rules in this area. The question really is how far we can go.

The capital proposals I have put to colleagues would continue the present initial disregard of £3,000, apply a tarrif income system on capital between £3,000 and £6,000, and exclude claimants from benefit with holdings above the £6,000 level. This would be part of a package of incentives which would provide less encouragement to run down capital and greater opportunities for the long term unemployed to work their way back to employment.

I do, however, see problems in going further on capital than my proposals. The greater the easement the more we end up creating the sort of benefit society which you comment we should try to avoid. My proposals would mean some increase in supplementary benefit costs and the numbers on benefit. There has to be a limit on how far this inevitable consequence of an easement of the rules would be acceptable. My judgement is that £6,000 - which to most people on modest incomes would seem like a sizeable sum of money - is the limit above which we really should not encourage people to look to supplementary benefit from the State.

The question is particularly relevant to housing benefit where there has been the widespread criticism of the present system that help goes too far up the income scale. There is in the present system a fairly generous treatment of capital compared to that now applying in supplementary benefit. That seems to me wrong and I propose to align the two rules. One of the attractions of common rules in this area is that overall the effect is to reduce reliance on means-testing. The housing benefit potential savings from my proposals are greater than the supplementary benefit costs and, overall, we would reduce the numbers on means-tested benefits. Adopting a more generous rule and applying it to housing benefit as well - as I think we will have to - starts to undermine our efforts to rein back expenditure on that benefit. I think my proposals represent a reasonable balance between encouraging sensible use of savings and combating too ready reliance on means-tested benefits.

I am copying this letter to the Prime Minister, the Chancellor of the Exchequer, the Secretary of State for Employment, the Minister without Portfolio and Sir Robert Armstrong.

Yours
Norman

NORMAN FOWLER

From: IAN WEBB
18 March 1985

MR CULPIN - IDT

MR LANG - CSO Press Office

cc List A

Chancellor
Sir P Middleton
Sir T Burns
Mr Cassell
Mr H Evans
Mr Lankester
Mr Collinson
Mr Folger
Miss Peirson
Mr Peretz
Mr D Andren
Mr Ward - CSO
Mr Wright - Bank of England
Mr Turnbull - No. 10

List B (distributed at 2.30pm, 18 March)

Chief Secretary
Financial Secretary
Economic Secretary
Minister of State
Mr Stibbard
Mr Spencer
Mr Cropper
Mr Lord
Mrs Hillier - Inland Revenue
Mr D Mitchell - Customs and Excise

BRIEFING FOR 18 MARCH PSBR PRESS NOTICE

The PSBR figures for February will be published at 2.30pm on 18 March. The provisional outturns, together with 1983-84 figures for April to February, are shown in Table 1. Cumulative figures for the PSBR and its components for 1983-84 and 1982-83 are shown in Table 2 overleaf.

Table 1: **Borrowing requirement outturns**

£ billion

	Apr-Feb 1983-84	Apr-Feb 1984-85	February 1985
Central government on own account	6.7	5.0	**-0.6**
Local authorities	0.2	1.4	**0.4**
Public corporations	0.6	1.2	**-**
PSBR	7.5	7.6	**-0.2**
Memo: CGBR (including borrowing for on-lending to LAs and PCs)	10.4	7.8	**-0.2**

Note: All figures are on the new definition. Figures may not sum precisely because of rounding.

Table 2: PUBLIC SECTOR BORROWING REQUIREMENT - Comparison with the last two years

Cumulative £ billion

	Central government on own account			Local authorities borrowing requirement			Public corporations borrowing requirement			Public sector borrowing requirement		
	1982-83	1983-84	1984-85	1982-83	1983-84	1984-85	1982-83	1983-84	1984-85	1982-83	1983-84	1984-85
Apr	1.0	0.9	**1.9**	0.3	0.5	**0.9**	-0.6	-0.2	**-0.4**	0.8	1.2	**2.4**
May	2.3	2.4	**3.2**	0.2	0.3	**0.8**	-0.6	-0.3	**-0.4**	1.8	2.4	**3.6**
Jun	3.3	3.7	**4.5**	-0.3	-0.1	**0.6**	-0.3	-0.4	**-0.5**	2.7	3.2	**4.6**
Jul	3.6	4.5	**5.0**	-0.3	-0.0	**0.8**	-0.2	-0.6	**-0.7**	3.1	3.9	**5.2**
Aug	4.6	5.7	**6.2**	-0.3	0.3	**1.4**	-0.2	-0.4	**-0.7**	4.2	5.6	**6.8**
Sep	4.2	6.6	**6.4**	-0.4	0.3	**1.3**	0.5	-0.0	**-0.3**	4.4	6.9	**7.4**
Oct	4.4	6.7	**6.8**	-0.4	0.3	**1.0**	0.7	0.1	**0.2**	4.6	7.1	**8.0**
Nov	5.7	8.3	**8.5**	-1.0	-0.2	**0.8**	0.8	0.4	**0.3**	5.5	8.5	**9.6**
Dec	7.2	9.1	**7.8**	-1.0	0.1	**1.2**	0.9	0.6	**1.2**	7.1	9.8	**10.2**
Jan	5.2	6.3	**5.6**	-1.2	0.1	**1.0**	1.0	0.7	**1.2**	5.1	7.1	**7.8**
Feb	5.8	6.7	**5.0**	-1.1	0.2	**1.4**	1.2	0.6	**1.2**	6.0	7.5	**7.6**
Mar	7.2	8.2		0.1	1.2		1.5	0.3		8.9	9.7	

Note: All figures are on the new definition. Figures may not sum precisely because of rounding.

CONFIDENTIAL AND PERSONAL
(Until 2.30pm on 18 March 1985)

2. The (provisional) PSBR for February shows a net repayment of debt of £0.2 billion. Forecasts of City analysts are for <u>net borrowing</u> of between £¼ billion and £1¼ billion, with an average of about £½ billion.

3. At £7.6 billion, the outturn for April – February is very close to the outturn for the same 11 months last year (Table 2).

4. The Q and A briefing below gives background and sets out the line to take on particular issues. Comparisons are between the first 11 months of 1984-85 and the same 11 months of 1983-84.

Q1. Comment on February PSBR?

Line to take

The figure for February is low in comparison with the same month in previous years, but PSBR is subject to erratic influences as well as seasonal variations. PSBR benefitted by around £¼ billion by changed accounting procedures on VAT (see Q14). Better to look at cumulative figures.

Q2. What is latest PSBR forecast for 1984-85? Is it over £9 billion?

Background

Most outside forecasts give a PSBR in the range £9½-10½ billion for 1984-85. Outturn for April-February is close to outturn for same period of 1983-84, and PSBR in whole of 1983-84 was £9.7 billion (on new definition).

Line to take

Tomorrow's Budget will give revised forecast for PSBR outturn. Many uncertainties involved in forecasting PSBR, reflecting huge flow of receipts and expenditure on both sides of account; comparison with 1983-84 not simple with, for example, the effects of the aftermath of the coal strike and increased oil revenues affecting borrowing towards the end of 1984-85.

See also Q7 on expenditure.

Q3. Effect of recent fall in exchange rate on oil revenues?

Line to take

Not had any significant effect on oil revenues in 1984-85 PRT in March now received.

Q4. Effect of higher interest rates?

Line to take

This will have increased some costs but also some receipts.

Q5. Effect of miners' strike on PSBR in 1984-85 ? in February ?

Background

Autumn Statement estimate, on assumption that strike ended at Christmas, was for a PSBR cost in 1984-85 of £1½ billion.

Line to take

Continuation of the strike to beginning of March will have increased Autumn Statement estimate. A revised figure will be given in the Budget.

Q6. What is the position on EC refunds ?

Background

The European Parliament voted on 10 October to release 1983 refund. The Commission announced on 18 October their Decisions on the allocation of the refund.

Line to take

- European Parliament has released 1983 refund, £545 million already received. The rest is expected to be received by the end of the financial year.
- On the other hand, the 1984 rebate (1 billion ECU) is not likely to be received in 1984-85 and this delay was taken into account in the Autumn Statement forecast.

Q7. Supply running at a high level ?

Background

Supply services were 7.4 per cent higher in April-February compared with the same eleven months in 1983-84. For 1984-85 as a whole, 1984 Budget forecast was about 5¾ per cent higher than 1983-84 outturn. The line to take gives a number of factors contributing to the increase. In particular, advanced EC contributions, not allowed for in 1984 Budget forecast, from Supply rather than Standing Services, so that Supply is increased and Standing Services reduced.

Line to take

Increase in these eleven months over the same period last year is running ahead of 1984 Budget forecast increase for whole year. Many factors affecting outturn to end-February, including higher payments to British Steel and the National Coal Board, payment of advanced EC contributions from Supply, and Housing Corporation loans being refinanced by grants earlier than expected. Forecast for whole year is now higher, and will be published in the Budget.

Q8. Effect of asset sales on PSBR ?

Background

Asset sales have now passed the Budget forecast of £1.9 billion. Receipts to end-February credited to the special assets sales programme are a little under £2.1 billion, including gross receipts from BT first call of £1506 million. Disposal of residual shareholding in British Aerospace announced on 15 January will take place in 1985-86, so will not affect 1984-85 PSBR.

Note: Not all privatisation receipts count as special sales of assets. For example, Jaguar (receipts retained by BL, so no direct effect on PSBR) and Sealink (receipts retained by BR).

Line to take

Asset sales of over £2 billion, more than the 1984 Budget forecast of £1.9 billion for 1984-85, have been successfully achieved.

Q9. What is effect of public service pay settlements on 1984-85 PSBR?

Background

Public expenditure plans for 1984-85 included provision of 3 per cent for increased pay and allowances of central government employees from due settlement dates (sa planning assumption made for 1985-86). Including review body awards, outturn so far averages close to 5 per cent. Only major settlement outstanding which affects 1984-85 expenditure is for local authority manuals (settlement due November 1984). No additional central government finance has been made available to meet costs of settlements since April 1984 except for the NHS.

Line to take

Cost of central government settlements is generally being absorbed within existing programmes; estimates of any additional public sector costs will be taken into account in Chancellor's Budget forecast of the PSBR.

Q10. What is the state of the Reserve ?

Background

Reserve set at £2¾ billion in 1984 Public Expenditure White Paper. The estimate of the planning total outturn given in the 1985 PEWP published last month was £128.1 billion (i.e. £1¾ billion up on 1984 PEWP plans) still based on an end December strike assumption. (The spring Supplementary Estimates announced on 14 February were broadly consistent with the estimated outturn of public expenditure plans given in the PEWP.)

Line to take

An updated figure for the estimated outturn will appear in the FSBR.

Q11. How do tax revenues generally compare with 1984 Budget forecast ?

Line to take

North Sea receipts in 1984-85 were forecast in the Autumn Statement to be around £1½ billion higher than in the 1984 Budget and other tax receipts around £½ billion lower. [No breakdown of latter shortfall between Inland Revenue and Customs and Excise taxes was given.] Nearly all the increase in oil receipts was due in March. Updated forecast will be given in the Budget.

Q12. Are Inland Revenue receipts on track?

Background

1984 Budget forecast (which did not include latest forecast of £1½ billion increase in oil receipts) was for increase in 1984-85 over 1983-84 of 10 per cent in Inland Revenue duties. Receipts in February were £4.5 billion, bringing the total for the period April - February to £45.3 billion, 9 per cent up on the same period last year.

Excluding Petroleum Revenue Tax, the increase is 8¼ per cent compared with a Budget forecast of 11¾ per cent for the year as a whole.

Line to take

Inland Revenue receipts in the year so far are running a little below the rate implied in the last Budget forecast for 1984-85 as a whole. The latest estimate for 1984-85 will be published tomorrow in the FSBR.

Q13. Are Customs and Excise revenues on track?

Background

The Budget forecast for 1984-85 Customs and Excise receipts was £35 billion. This represents an 11½ per cent increase on the 1983-84 outturn. For April to February receipts are 13.7 per cent higher than those for the corresponding period last year.

Line to take

Receipts to date are running slightly ahead of the Budget forecast. Latest estimates will be published in FSBR tomorrow. See Q14.

Q14. What has been the effect on Customs revenues of changed accounting for VAT?

Background

1984 Budget forecast was for £1.2 billion receipts in 1984-85 from accelerated VAT on imports.

Line to take

In each of December, January and February the additional receipts have been of the order £¾ billion, £½ billion and £¼ billion respectively.

Q15. Local authorities borrowing certain to exceed 1984 Budget forecast for 1984-85 ?

Background

Preliminary estimate is that local authorities borrowed £0.4 billion in February, bringing the total borrowing April to February to £1.4 billion. This compares with 1984 FSBR forecast of £1.3 billion for the year as a whole. Main reason why 1984-85 borrowing is likely to exceed FSBR figure is overspending by local authorities on capital expenditure. A second, but relatively minor, reason is the spill over from 1983-84 into 1984-85 of borrowing associated with high payments of home improvement grants in March 1984.

Line to take

Local authority borrowing is running at a high level compared with 1984 Budget forecast. This was reflected in the Autumn Statement forecast of the PSBR.

Q16. Public corporations' borrowing ?

Background

First estimate shows a small net repayment of debt by public corporations in February, giving total borrowing of £1.2 billion from April to February. 1984 Budget forecast was £0.6 billion.

Line to take

Public corporations have borrowed £1.2 billion April-February, compared with £0.7 billion over the same period last year. High borrowing over recent months is partially attributable to the coal strike, but it is not clear to what extent; public corporations' borrowing follows an erratic pattern, as illustrated by the contrast between the January and February outturn and those of previous months.

Q17. How does the Nigerian/Brazilian/other debtor countries' position affect the PSBR ?

Background

The effect is via ECGD. Higher payments will increase the CGBR and PSBR, but not the public expenditure planning total (and so there would not be a claim on the expenditure Reserve). ECGD's payments of claims under its guarantees are part of its gross trading surplus/deficit which in full national accounts terms is treated as revenue. (However, confusingly, this surplus/deficit is included under "supply services" in the tables attached to the press notice, because ECGD's activities are all vote-borne.) Claims payments are made by ECGD when debts are overdue, in accordance with the terms of its insurance policies, or when existing debts are rescheduled. When debts are refinanced, through a commercial bank loan guaranteed by ECGD, no direct payments are made by ECGD, although there is clearly a contingent liability.

Press reports of a £500 million impact on the PSBR in this financial year from Nigerian developments are inaccurate. ECGD estimates that the total insured short-term arrears are about £450 million, but these would take time to pay out. (About £200 million will be paid this year.) And a multilateral agreement on a refinancing deal would avoid any further direct payments and recoup those already made. (This has now happened for Brazil and about £100 million has been recouped).

Line to take

The PSBR (but not the public expenditure planning total) is affected if ECGD's guarantees are called. Claims payments by ECGD are running higher than forecast in the Main Estimate (reflected in the increase of £186 million in ECGD's trading activities shown in the winter supplementaries - ECGD had no Spring supplementaries). Since no refinancing deal has been put in place for Nigeria, there is some impact on the PSBR for 1984-85, but not as much as press speculation.

J. H Clark

pp. Ian Webb (ext 5712)
PSF Division, HM Treasury

for [illegible]

248/008

SECRET

ECONOMIC SECRETARY TO THE TREASURY

FROM: A M ELLIS
DATE: 18 March 1985

PS/CHANCELLOR

cc PS/Chief Secretary
PS/Financial Secretary
PS/Minister of State
PS/Sir P Middleton
PS/Sir T Burns
Mr Bailey
Mr Monck
Mr Kemp
Mr Battishill
Mr Odling-Smee
Ms Seammen
Mr Culpin
Mr Folger
Mr Mercer

EMPLOYMENT WHITE PAPER

You asked for Ministers' comments on Mr Monck's submission of 13 March which questioned the merits of having any White Paper on employment at all.

2. The Economic Secretary certainly agrees that the White Paper in its present form is unsuitable for publication and has commented that the observation in the draft reply that the 'purpose and message are not entirely clear' is a damning one. Until the Department of Employment have focused on, and satisfactorily answered, this question he would not recommend agreement to publication.

AE

A M ELLIS

FROM: R A L LORD
DATE: 19 March 1985

CHANCELLOR

cc: Mr Monck
Mr Cropper
Mr D Davies

EMPLOYMENT WHITE PAPER

I agree with Mr Monck that the draft Employment White paper is not very satisfactory as it stands. I doubt, however, that it will do any harm.

2. Strategically, there seems a good case for setting out the Government's analysis of unemployment and its strategy for dealing with it (if that is what the White paper were to do). Tactically, a White Paper in the month or so after the Budget would help to support the message of a Budget for jobs.

3. I would therefore counsel postponement of the White Paper and urgent additional work on it rather than its suppression.

4. Criticisms of the draft might include:

(a) the material is still organised rather confusingly;

(b) there is not much evidence of new thinking (that might not matter if we at least had a coherent expression of old thinking);

(c) a White Paper should surely aim to be a formal and comprehensive expression of the Government's policy towards a particular issue, and for that the tone of the document is wrong - too polemical and inclined to hyperbole.

These defects can probably be largely remedied if enough collective pressure is brought to bear and enough official and ministerial time expended. On an area of such central concern to the Government, the effort may be worth making.

RL

R A L LORD

SECRET

From: H J Davies

Date: 19 March 1985

CHANCELLOR

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Sir Peter Middleton
Mr Bailey
Sir T Burns
Mr Battishill
Mr Odling-Smee
Mr Monck
Mr Cropper
Mr Lord

EMPLOYMENT WHITE PAPER

You asked for comments on the latest draft of the Employment White Paper. You are discussing it in No.10 tomorrow.

2. I understand that Mr King will try to "get at" you beforehand.

3. So far Treasury officials' comments have been sent over to the Department of Employment. They have taken account of some of the detailed drafting points, but not adjusted the structure of the paper as suggested.

4. I think there are a lot of difficulties here, on timing, content and on the whole purpose of the paper.

Timing

5. Mr King thinks that publication has been definitively agreed for 28 March. I understand from Mr Monck that you are not certain that this was agreed. Although there are clearly interrelationships between the publication of this and other documents I think there is a strong case, given the disagreements which still exist, for trying to postpone the publication somewhat.

Purpose

6. I understand from Department of Employment that the target market for this document is:

- Backbenchers.

- Commentators.

- The party in the country.

7. I think that they have set themselves a tall order. In its present form the paper is too long for backbenchers, too vague for the party in the country and too polemical for commentators. But I presume that there is no point in trying to reopen the whole question of publication.

8. There is, however, some point in discussing the appropriate tone to adopt in the paper. In the Budget Speech and the Budget Broadcast we are now working on you have adopted a frank tone on the whole question of unemployment. The difficulty with this document is that although its existence indicates the Government's recognition of the seriousness of the problem it mixes analysis prescription and exhortation throughout. It does not read to me like a normal White Paper and lacks something of the neutral authority which such a document could have. Clearly that is because it is partly targetted as a political document in the latter case it fails also in that it is less punchy and party political than it would be were it to be issued by Central Office. What I am saying, is that I think it falls between two stools in its present form.

Structure

9. But even given the Department's objectives and the basic content of the paper the structure could be significantly improved and it could be made into a much more useful document than it is. At the moment you will see that Sections 2 and

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3 are entitled the strategy for jobs and the way forward which is a confusing distinction. A section on unit labour costs is included in the way forward, where it would seem to me to be part of the diagnosis of our employment problem. The Department of Employment does acknowledge that there is a structural problem here. And there is some willingness to think of changes. But I fear that they need to be fairly radical in order to make much difference.

10. I attach a brief reworking of what I think a more appropriate structure would be, though I recognise that it might be difficult to sell this to the Department of Employment at this relatively late stage.

Next Steps

11. You will wish to consider before seeing Mr King whether you will want to push for postponement of publication. One minor point in this connection is that you have not referred to the Employment White Paper in your Budget Speech, which might argue that it would be odd to publish it very quickly thereafter.

12. You should also consider whether you think it worthwhile to push for a more radical redraft of the paper. If you do the three key points to make to Mr King are:

- We need to ensure that the macroeconomic framework is put at the beginning and not conceived as a response to unemployment which it now could be read as being

- The existing structure is difficult to follow, particularly if we want it to reach a wider political audience

- The document might carry more weight if it began with an extended analysis of the problem in more neutral terms and demonstrated that the

SECRET

Government's policy flowed from that analysis.

HJD

H J DAVIES

SECRET

EMPLOYMENT WHITE PAPER

Possible Revised Structure

1. **Introduction**

Unemployment is a very serious problem for the country, though not purely a British problem. Not a problem of demand management. This is an out-dated approach. If it were a demand problem it would be easy to solve.

Need to look at the roots of unemployment in the UK, at the changing market and technological environments etc and to identify the appropriate policy response.

[Ie most of their part 1 with the macroeconomic policy woven in more coherently.]

2. **The problem**

Analysis of changing trends in the labour force [Chapter 3] the growth of unemployment both here and overseas.

Hypothesis about this growth and the still relatively poor performance of the UK. Including our poor performance on pay [from Chapter 2] and our unit labour cost problem [from Chapter 7].

Analysis of labour market problems in the UK contributing to unemployment difficulties [Chapter 5].

3. **The Government's response**

The Government's response is in three parts (Section 2 include both measures already taken and those planned]

- Macroeconomic policy - recapitulation of the argument for sound money as a necessary but not sufficient condition of a healthy labour market

- Measures to improve the functioning of markets [parts of Chapter 7]

- Measures to improve the supply and quality of labour and to elevate the worst effects of unemployment [Chapters 6 and 8]

4. **Conclusion**

Recapitulation of main themes and recommendations for needed actions by others than Government (Trades Unions, employers etc).

CHANCELLOR OF THE EXCHEQUER

HONI SOIT QUI MAL Y PENSE

C/

You didn't have time to comment on the draft of the White Paper circulated on 6 March. At DE's request, our officials passed comments to theirs, without committing you in any way. MST's & EST's comments relate to that draft.

Mr Tebbit clearly wasn't very keen on the whole enterprise but other departments haven't commented substantively (They were represented on the group which drafted the document)

Mr King has now sent round a revised draft with which officials & Howard (see note below) are still unhappy. Mr Tebbit wrote today & seems broadly content.

Nick thinks that if you feel strongly, your best bet is to have a

PTO

word with Mr Tebbit before the

meeting but it doesn't look

too promising to me.

MGM

19/3

P.S. See separate folder on Wages

Councils

198/17

SECRET

Ch.

PM has said she is broadly happy with the latest draft

RL 20/3

FROM: **N MONCK**
DATE: **19 March 1985**

CHANCELLOR

cc Chief Secretary
Financial Secretary
Economic Secretary
Minister of State
Sir P Middleton
Mr Bailey
Sir T Burns
Mr Kemp
Mr Battishill
Mr Odling-Smee
Ms Seammen
Mr Culpin
Mr Folger
Mr Riley
Mr Mercer
Mr Gilhooly
Mr Cropper
Mr Lord
Mr H Davies

C

Question for you in final para of Nick's note. Answer if poss' pl early tomorrow.

RO 19/3

PS. See also Rodney's minute (just arrived).

EMPLOYMENT WHITE PAPER

The Prime Minister's meeting tomorrow evening is a follow-up to the meeting on "Employment Related Policy Announcement" recorded in Mr Turnbull's letter of 11 March and the attached timetable. The main item is Mr King's White Paper: he circulated a new version on 15 March. Some of the other forthcoming documents may, however, come up at the end.

2. My submission of 13 March and the draft covering letter said that officials found the existing text unsatisfactory and more likely to damage the Government than to help it; its purpose and message and hence the logic of the three-part structure were not clear; I suggested that the letter should record reservations and postpone reaching a conclusion on advantages and disadvantages of going ahead until you saw the new text. The Economic Secretary and the Minister of State do not like the White Paper. Mr Davies is sending you a separate note with the political advisors' views.

3. DE have seen officials' comments, but no one else has. DE have taken quite a lot of our less important drafting amendments. But they have not clarified the message or improved the structure - our two main points. DE officials say the purpose of the White Paper is to show Government supporters that the Government has a coherent set of policies and is not just in the "hole-plugging and lecturing business". On the other hand Mr King does not like taking macro-economic policy as the starting point. I doubt if it is possible to square this circle convincingly.

4. Despite these problems, I understand, that the Prime Minister has meanwhile become quite enthusiastic about the draft White Paper. Mr Tebbit may be briefed to support you. But Lord Young will not, provided his White Paper can be linked in with Sir Keith Joseph's White Paper on schools.

Objectives

5. Sir Peter Middleton held a meeting this morning about the draft White Paper. It was agreed that the best outcome would be to abandon it. But that will now be very difficult to achieve.

6. It is not a realistic option for you to distance yourself from the White Paper so soon after a "Budget for jobs". So if it goes ahead, you will want to insist on improving it. That means postponement. To publish on the 28th means that comments have to be in by noon on Thursday morning of this week.

7. Postponement will be difficult partly because of the interaction with the timing of the Green Paper on the 14 to 18 age group. I gather Lord Young may now reluctantly accept Tuesday 2 April but he will not want to go further.

8. So either abandonment or postponement is going to be difficult to get (although the 14 to 18 White Paper could in our view come before Mr King's White Paper, he will resist

it strongly unless he is convinced that is the only way he can get his White Paper out).

9. Most, though not all, of the points to make below could be used either in support of abandonment or of postponement/improvement.

Points to Make

10. You could draw on the following points:

a) the Budget has prevented you from looking carefully at the draft White Paper;

b) the draft White Paper attempts something very difficult indeed (and perhaps impossible) and does not seem to you to pull it off. It does not have a clear theme which explains why unemployment is high and how it will come down;

c) it is not going to win any converts among commentators or the public; there is a risk that it will create damage by giving opponents a chance to argue that the Government does not have a credible strategy towards unemployment; and it is not clear that Backbenchers etc will be encouraged or better equipped as a result of it;

d) as Mr Tebbit has pointed out, the Government must not seem to accept that it can deal with unemployment unaided. But the lists of Government measures point the other way and prompt the question why there is still a problem;

e) the White Paper does not give a clear message about what businesses and employees should do to complement the Government's actions. [The lack of policy weapons to bring about early improvements on "pay and jobs" lines is bound to be a weakness of a comprehensive White Paper of this kind.]

f) It would at least be sensible to see how the Budget measures go down before deciding how to present them in the White Paper. At the very least postponement is desirable.

Specific Improvements in the Draft

If the White Paper is to go ahead, it should have an early chapter meeting the arguments that demand is inadequate head-on and explaining the link between prices and pay - as a key aspect of labour market adaptability - and jobs. It would explain the Government's macro-economic policy and repeat your NEDC pledge, as in the Budget speech. It would be worthwhile for you to read Mr Odling-Smee's first shot at Chapter 2 attached to my submission of 13 March.

11. The rest of the White Paper should be devoted exclusively to the labour market with references to macro-economic policy removed from chapter 4 and to demand removed from chapter 5. Apart from the introduction, the remaining chapters could be:

- "employment today" - trends in the labour market (present chapter 3)

- a summary of the changes needed in the labour market (merger of present chapters 4 and 5)

- three chapters on specific aspects:

  labour market flexibility and pay (drawing on present chapter 7)

  training (present chapter 6)

help for the unemployed (present chapter 8).

12. All this was suggested in our hurried comments of 13 March and will take a bit of time to work up.

Wages Councils Consultative Document

13 The Prime Minister's preference is for this to come out with the White Paper. If she sticks to that and you succeed in postponing the White Paper, Wages Councils would be delayed too. From your point of view, provided Mr King accepts your amendments, it would be preferable for this document to come out this Thursday, the day on which Mr King will speak in the Budget Debate. But you may not want to raise this.

14 to 18 Age Group White Paper

14 The drafts going round between officials are shaping up. But a version should now be circulated to Ministers as soon as possible. Tactically it may be best to avoid expressing a view on the date of publication, though you could accept that this could precede the Employment White Paper if you succeed in getting the latter postponed to allow time for improvement.

Mr Fowler's Green Paper and Yours on Personal Tax

15 If you have been able to talk to Mr Fowler about them, you might point out that the contents of these two papers will clearly need to be compatible. Since, for public expenditure reasons, we do not want Mr Fowler's Green Paper to slip, you may want to ask the Inland Revenue to accelerate the drafting of your Green Paper, though the scope for this will depend on the ground it has to cover.

Conclusions

16. a) Abandonment of the White Paper would be preferable, as it may not be possible to produce a convincing one. But unless Mr Tebbit supports you, it is unlikely to be obtainable. The useful information it contains could be published in some other - less comprehensive-form;

b) if so, you will want to press for postponement to allow time for the extensive improvements that are needed (drawing on paras 10 to 11). The 14-18 and Schools White Papers could still come out <u>before</u> the King White Paper.

c) you may want to make the points in paras 13-15 above, particularly 15.

17. If Ministers go for publication of the White Paper on Thursday, the timetable would be a crazy one with a deadline for comments at noon on Thursday, the day after the Prime Minister's meeting. It might be sensible to get comments designed to minimise damage over to DE tomorrow, if necessary before you have seen them but of course making that status clear. Do you want us to do that?

NM

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SECRET

DEPARTMENT OF TRADE AND INDUSTRY
1-19 VICTORIA STREET
LONDON SW1H 0ET
TELEPHONE DIRECT LINE 01-215 5422
SWITCHBOARD 01-215 7877

Secretary of State for Trade and Industry

19 March 1985

CH/EXCHEQUER
REC. 19 MAR 1985
ACTION Mr Monck
COPIES TO CST, FST, MST, EST; Sir P. Middleton; Mr Bailey; Sir T. Burns; Mr Battishill; Mr Cropper; Mr Lord

Rt Hon Tom King MP
Secretary of State for Employment
Department of Employment
Caxton House
Tothill Street
London SW1

D Tom,

EMPLOYMENT WHITE PAPER

I agree that the latest draft of the Employment White Paper is for the most part a timely and effective statement of our view. But I should still like to see in it a section explicitly setting out why the Government rejects particular alternatives often advanced as a means of combatting unemployment: why the artificial stimulation of demand by Government will not work, why inflation causes unemployment, why infrastructure spend, unless economically sound, will not generate jobs, etc. I recall that such a section was included in the draft which was circulated before Christmas and I suggest that officials be instructed to produce a shorter and sharper version of that, for inclusion in section 4 of the present draft.

2 Finally, I have seen your recent exchange of letters with David Young about the timing of publication of the White Paper. I am inclined to agree with David that it would be better to publish on, say, 2 April than on 28 March - that is to say, after instead of before publication of the 'burdens on business' scrutiny report. This would be logical, since as you know the burdens report identifies options for action on some points on which you wil be announcing decisions.

Yours

Norman

NORMAN TEBBIT

Copies of this letter go to the Lord President, Nigel Lawson, Keith Joseph, Patrick Jenkin, Norman Fowler David Young and Sir Robert Armstrong

JH1CCX

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CONFIDENTIAL

Sir Ry

CHIEF SECRETARY TO THE TREASURY

FROM: R J BROADBENT

DATE: 19 March 1985

MR PIRIE

cc: Chancellor
FST
EST
MST
Sir Peter Middleton
Mr Bailey
Mr Anson
Mr Cassell
Mr Byatt
Mr Scholar
Mr Jameson
Mr Battishill
Mr M L Williams
Mr H A Hall
Mr Peretz
Ms Spencer
Mr Lord

F PES: partic. progs.

SALES OF LOCAL AUTHORITY MORTGAGES

The Chief Secretary was grateful for your minute of 15 March. He agrees in the light of the relatively modest scale of refinancing which appears to be in prospect that no immediate action is needed. He would be grateful if you would keep the position under review.

2 The Chief Secretary agrees too that there is even less point in trying publicly to correct the Secretary of State's unfortunate intervention in the debate on 13 March. He has commented that a public statement would only serve to highlight the Government's impotence in this field. He would rather ensure that the new controls being discussed for 1986-87 should if possible cover these transactions.

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3 He is concerned, however, that the Secretary of State for Wales' remarks, which were not cleared with him, should not be allowed to pass without comment within Government. He would be grateful if you would let him have a short draft letter underlining the need to avoid encouraging these transactions. He thinks that the draft will need to be tactful since the Secretary of State considers his response to the debate to have been very successful.

R J BROADBENT
Private Secretary

From: IAN WEBB
XX March 1985

MR CULPIN - IDT

MR LANG - CSO Press Office

cc List A

Chancellor
Sir P Middleton
Sir T Burns
Mr Cassell
Mr H Evans
Mr Lankester
Mr Collinson
Mr Folger
Miss Peirson
Mr Peretz
Mr D Andren
Mr Ward - CSO
Mr Wright - Bank of England
Mr Turnbull - No. 10

List B (distributed at 2.30pm, 18 March)

Chief Secretary
Financial Secretary
Economic Secretary
Minister of State
Mr Stibbard
Mr Spencer
Mr Cropper
Mr Lord
Mrs Hillier - Inland Revenue
Mr D Mitchell - Customs and Excise

DRAFT BRIEFING FOR 18 MARCH PSBR PRESS NOTICE

The PSBR figures for February will be published at 2.30pm on 18 March. The provisional outturns, together with 1983-84 figures for April to February, are shown in Table 1. Cumulative figures for the PSBR and its components for 1983-84 and 1982-83 are shown in Table 2 overleaf.

Table 1: Borrowing requirement outturns

£ billion

	Apr-Feb 1983-84	Apr-Feb 1984-85	February 1985
Central government on own account	6.7	5.0	**-0.6**
Local authorities	0.2	1.4	**0.4**
Public corporations	0.6	1.2	-
PSBR	7.5	7.6	**-0.2**
Memo: CGBR (including borrowing for on-lending to LAs and PCs)	10.4	7.8	**-0.2**

Note: All figures are on the new definition. Figures may not sum precisely because of rounding.

Table 2: **PUBLIC SECTOR BORROWING REQUIREMENT – Comparison with the last two years**

Cumulative £ billion

	Central government on own account			Local authorities borrowing requirement			Public corporations borrowing requirement			Public sector borrowing requirement		
	1982–83	1983–84	1984–85	1982–83	1983–84	1984–85	1982–83	1983–84	1984–85	1982–83	1983–84	1984–85
Apr	1.0	0.9	**1.9**	0.3	0.5	**0.9**	−0.6	−0.2	**−0.4**	0.8	1.2	**2.4**
May	2.3	2.4	**3.2**	0.2	0.3	**0.8**	−0.6	−0.3	**−0.4**	1.8	2.4	**3.6**
Jun	3.3	3.7	**4.5**	−0.3	−0.1	**0.6**	−0.3	−0.4	**−0.5**	2.7	3.2	**4.6**
Jul	3.6	4.5	**5.0**	−0.3	−0.0	**0.8**	−0.2	−0.6	**−0.7**	3.1	3.9	**5.2**
Aug	4.6	5.7	**6.2**	−0.3	0.3	**1.4**	−0.2	−0.4	**−0.7**	4.2	5.6	**6.8**
Sep	4.2	6.6	**6.4**	−0.4	0.3	**1.3**	0.5	−0.0	**−0.3**	4.4	6.9	**7.4**
Oct	4.4	6.7	**6.8**	−0.4	0.3	**1.0**	0.7	0.1	**0.2**	4.6	7.1	**8.0**
Nov	5.7	8.3	**8.5**	−1.0	−0.2	**0.8**	0.8	0.4	**0.3**	5.5	8.5	**9.6**
Dec	7.2	9.1	**7.8**	−1.0	0.1	**1.2**	0.9	0.6	**1.2**	7.1	9.8	**10.2**
Jan	5.2	6.3	**5.6**	−1.2	0.1	**1.0**	1.0	0.7	**1.2**	5.1	7.1	**7.8**
Feb	5.8	6.7	**5.0**	−1.1	0.2	**1.4**	1.2	0.6	**1.2**	6.0	7.5	**7.6**
Mar	7.2	8.2		0.1	1.2		1.5	0.3		8.9	9.7	

Note: All figures are on the new definition. Figures may not sum precisely because of rounding.

CONFIDENTIAL AND PERSONAL
(DRAFT)

2. The (provisional) PSBR for February shows a net repayment of debt of £0.2 billion. Forecasts of City analysts are for net borrowing of between £¼ billion and £1¼ billion, with an average of about £½ billion.

3. At £7.6 billion, the outturn for April – February is very close to the outturn for the same 11 months last year (Table 2).

4. The Q and A briefing below gives background and sets out the line to take on particular issues. Comparisons are between the first 11 months of 1984-85 and the same 11 months of 1983-84.

Q1. Comment on February PSBR?

Line to take

The figure for February is low in comparison with the same month in previous years, but PSBR is subject to erratic influences as well as seasonal variations. PSBR benefitted by around £¼ billion by changed accounting procedures on VAT (see Q14). Better to look at cumulative figures.

Q2. What is latest PSBR forecast for 1984-85? Is it over £9 billion?

Background

Most outside forecasts give a PSBR in the range £9½-10½ billion for 1984-85. Outturn for April-February is close to outturn for same period of 1983-84, and PSBR in whole of 1983-84 was £9.7 billion (on new definition).

Line to take

Tomorrow's Budget will give revised forecast for PSBR outturn. Many uncertainties involved in forecasting PSBR, reflecting huge flow of receipts and expenditure on both sides of account; comparison with 1983-84 not simple with, for example, the effects of the aftermath of the coal strike and increased oil revenues affecting borrowing towards the end of 1984-85.

See also Q7 on expenditure.

Q3. Effect of recent fall in exchange rate on oil revenues?

Line to take

Not had any significant effect on oil revenues in 1984-85 PRT in March now received.

Q4. Effect of higher interest rates?

Line to take

This will have increased some costs but also some receipts.

Q5. Effect of miners' strike on PSBR in 1984-85 ? in February ?

Background

Autumn Statement estimate, on assumption that strike ended at Christmas, was for a PSBR cost in 1984-85 of £1½ billion.

Line to take

Continuation of the strike to beginning of March will have increased Autumn Statement estimate. A revised figure will be given in the Budget.

Q6. What is the position on EC refunds ?

Background

The European Parliament voted on 10 October to release 1983 refund. The Commission announced on 18 October their Decisions on the allocation of the refund.

Line to take

- European Parliament has released 1983 refund, £545 million already received. The rest is expected to be received by the end of the financial year.
- On the other hand, the 1984 rebate (1 billion ECU) is not likely to be received in 1984-85 and this delay was taken into account in the Autumn Statement forecast.

Q7. Supply running at a high level ?

Background

Supply services were 7.4 per cent higher in April-February compared with the same eleven months in 1983-84. For 1984-85 as a whole, 1984 Budget forecast was about 5¾ per cent higher than 1983-84 outturn. The line to take gives a number of factors contributing to the increase. In particular, advanced EC contributions, not allowed for in 1984 Budget forecast, from Supply rather than Standing Services, so that Supply is increased and Standing Services reduced.

Line to take

Increase in these eleven months over the same period last year is running ahead of 1984 Budget forecast increase for whole year. Many factors affecting outturn to end-February, including higher payments to British Steel and the National Coal Board, payment of advanced EC contributions from Supply, and Housing Corporation loans being refinanced by grants earlier than expected. Forecast for whole year is now higher, and will be published in the Budget.

Q8. Effect of asset sales on PSBR ?

Background

Asset sales have now passed the Budget forecast of £1.9 billion. Receipts to end-February credited to the special assets sales programme are a little under £2.1 billion, including gross receipts from BT first call of £1506 million. Disposal of residual shareholding in British Aerospace announced on 15 January will take place in 1985-86, so will not affect 1984-85 PSBR.

Note: Not all privatisation receipts count as special sales of assets. For example, Jaguar (receipts retained by BL, so no direct effect on PSBR) and Sealink (receipts retained by BR).

Line to take

Asset sales of over £2 billion, more than the 1984 Budget forecast of £1.9 billion for 1984-85, have been successfully achieved.

Q9. What is effect of public service pay settlements on 1984-85 PSBR?

Background

Public expenditure plans for 1984-85 included provision of 3 per cent for increased pay and allowances of central government employees from due settlement dates (same planning assumption made for 1985-86). Including review body awards, outturn so far averages close to 5 per cent. Only major settlement outstanding which affects 1984-85 expenditure is for local authority manuals (settlement due November 1984). No additional central government finance has been made available to meet costs of settlements since April 1984 except for the NHS.

Line to take

Cost of central government settlements is generally being absorbed within existing programmes; estimates of any additional public sector costs will be taken into account in Chancellor's Budget forecast of the PSBR.

Q10. What is the state of the Reserve ?

Background

Reserve set at £2¾ billion in 1984 Public Expenditure White Paper. The estimate of the planning total outturn given in the 1985 PEWP published last month was £128.1 billion (i.e. £1¾ billion up on 1984 PEWP plans) still based on an end December strike assumption. (The spring Supplementary Estimates announced on 14 February were broadly consistent with the estimated outturn of public expenditure plans given in the PEWP.)

Line to take

An updated figure for the estimated outturn will appear in the FSBR.

Q11. How do tax revenues generally compare with 1984 Budget forecast ?

Line to take

North Sea receipts in 1984-85 were forecast in the Autumn Statement to be around £1½ billion higher than in the 1984 Budget and other tax receipts around £½ billion lower. [No breakdown of latter shortfall between Inland Revenue and Customs and Excise taxes was given.] Nearly all the increase in oil receipts was due in March. Updated forecast will be given in the Budget.

Q12. Are Inland Revenue receipts on track?

Background

1984 Budget forecast (which did not include latest forecast of £1½ billion increase in oil receipts) was for increase in 1984-85 over 1983-84 of 10 per cent in Inland Revenue duties. Receipts in February were £4.5 billion, bringing the total for the period April - February to £45.3 billion, 9 per cent up on the same period last year.

Excluding Petroleum Revenue Tax, the increase is 8¼ per cent compared with a Budget forecast of 11¾ per cent for the year as a whole.

Line to take

Inland Revenue receipts in the year so far are running a little below the rate implied in the last Budget forecast for 1984-85 as a whole. The latest estimate for 1984-85 will be published tomorrow in the FSBR.

Q13. Are Customs and Excise revenues on track?

Background

The Budget forecast for 1984-85 Customs and Excise receipts was £35 billion. This represents an 11½ per cent increase on the 1983-84 outturn. For April to February receipts are 13.7 per cent higher than those for the corresponding period last year.

Line to take

Receipts to date are running slightly ahead of the Budget forecast. Latest estimates will be published in FSBR tomorrow. See Q14.

Q14. What has been the effect on Customs revenues of changed accounting for VAT?

Background

1984 Budget forecast was for £1.2 billion receipts in 1984-85 from accelerated VAT on imports.

Line to take

In each of December, January and February the additional receipts have been of the order £¾ billion, £½ billion and £¼ billion respectively.

Q15. Local authorities borrowing certain to exceed 1984 Budget forecast for 1984-85 ?

Background

Preliminary estimate is that local authorities borrowed £0.4 billion in February, bringing the total borrowing April to February to £1.4 billion. This compares with 1984 FSBR forecast of £1.3 billion for the year as a whole. Main reason why 1984-85 borrowing is likely to exceed FSBR figure is overspending by local authorities on capital expenditure. A second, but relatively minor, reason is the spill over from 1983-84 into 1984-85 of borrowing associated with high payments of home improvement grants in March 1984.

Line to take

Local authority borrowing is running at a high level compared with 1984 Budget forecast. This was reflected in the Autumn Statement forecast of the PSBR.

Q16. Public corporations' borrowing ?

Background

First estimate shows a small net repayment of debt by public corporations in February, giving total borrowing of £1.2 billion from April to February. 1984 Budget forecast was £0.6 billion.

Line to take

Public corporations have borrowed £1.2 billion April-February, compared with £0.7 billion over the same period last year. High borrowing over recent months is partially attributable to the coal strike, but it is not clear to what extent; public corporations' borrowing follows an erratic pattern, as illustrated by the contrast between the January and February outturn and those of previous months.

Q17. How does the Nigerian/Brazilian/other debtor countries' position affect the PSBR ?

Background

The effect is via ECGD. Higher payments will increase the CGBR and PSBR, but not the public expenditure planning total (and so there would not be a claim on the expenditure Reserve). ECGD's payments of claims under its guarantees are part of its gross trading surplus/deficit which in full national accounts terms is treated as revenue. (However, confusingly, this surplus/deficit is included under "supply services" in the tables attached to the press notice, because ECGD's activities are all vote-borne.) Claims payments are made by ECGD when debts are overdue, in accordance with the terms of its insurance policies, or when existing debts are rescheduled. When debts are refinanced, through a commercial bank loan guaranteed by ECGD, no direct payments are made by ECGD, although there is clearly a contingent liability.

Press reports of a £500 million impact on the PSBR in this financial year from Nigerian developments are inaccurate. ECGD estimates that the total insured short-term arrears are about £450 million, but these would take time to pay out. (About £200 million will be paid this year.) And a multilateral agreement on a refinancing deal would avoid any further direct payments and recoup those already made. (This has now happened for Brazil and about £100 million has been recouped).

<u>Line to take</u>

The PSBR (but not the public expenditure planning total) is affected if ECGD's guarantees are called. Claims payments by ECGD are running higher than forecast in the Main Estimate (reflected in the increase of £186 million in ECGD's trading activities shown in the winter supplementaries - ECGD had no Spring supplementaries). Since no refinancing deal has been put in place for Nigeria, there is some impact on the PSBR for 1984-85, but not as much as press speculation.

Ian Webb (ext 5712)
PSF Division, HM Treasury

From: R J Devereux

Date: 2 April 1985

Reassuring! JC.

1. MR CASSELL

2. CHANCELLOR OF THE EXCHEQUER

C. To note. PWO 2/4

cc Chief Secretary
Financial Secretary
Economic Secretary
Minister of State
Sir P Middleton
Mr Bailey
Sir T Burns
Mr Battishill
Mr H Evans
Mr Lankester
Mr Scholar
Mr Collinson
Miss Peirson o/r
Mr M Hall
Mr Peretz
Mr Stibbard
Mr O'Donnell
Mr Powell
Dr I Webb

REPORT ON CENTRAL GOVERNMENT TRANSACTIONS AT THE END OF MARCH

The preliminary estimate of the CGBR in 1984/85 is £9.9 billion, and the estimate of borrowing by central government on its own account - CGBR(0) - is £6.4 billion. These figures are not yet firm and may change with later information before publication on 18 April in the monthly press notice on the PSBR.

2. The CGBR(0) outturn is £0.4 billion lower than forecast in the Financial Statement and Budget Report on 19 March. The main factors appear to be higher Customs and Excise receipts and lower Supply expenditure, partly offset by a small shortfall on Inland Revenue receipts and a lower surplus on the National Insurance Fund.

3. On-lending to local authorities was higher than forcast partly because of a cut in the PWLB lending rate in the last week of March. On-lending to public corporations was lower than expected because of lower borrowing by the National Coal Board.

4. The first estimate of the PSBR outturn for 1984/85 will be available on ~~Wednesday 10~~ Thursday 11 April, and, as usual, a detailed analysis of the figures will be included in the monthly Ministerial note in two weeks' time.

R J DEVEREUX

CONFIDENTIAL

CENTRAL GOVERNMENT TRANSACTIONS(1)

£ million

	Inland Revenue taxes(2)	Customs and Excise	Net Lending (i) LAs	Net Lending (ii) PCs(3)	Other	CGBR
Financial year to 31 March 1985 - outturn(4)	+50,350	+35,502	- 3,325	- 146	-92,256	- 9,875
Financial year to 31 March 1984 - outturn	+45,926	+31,435	- 3,431	- 669	-85,545	-12,284
% increase on last year	9.6	12.9			7.8	
'Latest estimate' for 1984-85 in FSBR (rounded figures)	+50,500	+35,300	- 2,900	- 400	-92,600	-10,100
% increase on last year	10.0	12.3			8.2	
Calendar Month of March 1985 - outturn(4)	+ 5,091	+ 2,872	- 760	+ 28	- 9.337	- 2,106
- difference from forecast in PSBR note of 15 March 1985 and the FSBR	- 150	+ 202	- 421	+ 257	+ 356	+ 244

(1) + indicates a receipt, net receipt, or difference which reduces the CGBR
- indicates a payment, net payment, or difference which increases the CGBR

(2) Excludes National Insurance contributions

(3) Includes PDC issues and issues under Section 18 of the Iron and Steel Act 1975

(4) Preliminary estimate, subject to revision.

SECRET

copy no: 2 of 4

bf with advice + back papers pl.

CH/EXCHEQUER

REC.	10 APR 1985
ACTION	MR ROBSON
COPIES TO	SIR P. MIDDLETON
	MR CASSELL

11/4

01 211 7214

Robin Butler Esq
Principal Private Secretary to the
Prime Minister
10 Downing Street
London
SW1

10 April 1985

Dear Robin

Thank you for your letter of 26 March, which recorded a remit to my Secretary of State to consider, in consultation with the Chancellor, methods and timing of a move to take North Sea royalties in cash rather than in oil.

My Secretary of State will certainly pursue this matter. His understanding, however, is that it was agreed that any switch to cash should take place in the longer term, and when the Chancellor could accommodate the adverse impact this would have on the PSBR.

A very early change would call in question the case for setting up the new Agency, as announced to the House on 13 March. It would undoubtedly stir up fresh anxieties about security of supply which the Minister of State was at pains to allay at the time of the statement. It would also add to our problems with BNOC staff. The announcement about the Agency and its functions was, after all, agreed after careful consideration between the Treasury and the Department of Energy of the possibility of moving in the immediate future to cash rather than oil.

My Secretary of State will nevertheless be ready to review further the question of royalty oil once the new Agency has been successfully established and we have had some experience of their operations in this oil. And he certainly intends that the legislation should keep open the possibility of change.

I am copying this letter to Rachel Lomax and Len Appleyard.

Yours sincerely
Rachel Lomax

M F REIDY
Private Secretary

SECRET

CONFIDENTIAL & PERSONAL

FROM: MISS M E PEIRSON
DATE: 11 April 1985

I think this can be regarded as a satisfactory outcome.
11/4.

or a mistake

1. MR CASSELL
2. CHANCELLOR OF THE EXCHEQUER

cc Sir P Middleton
Sir T Burns
Mr H P Evans
Mr Battishill
Mr Lankester
Mr Devereux
Dr I Webb
Mr Wells - CSO

Ch The supposedly terrible money figures must reflect a surge in bank lending – this is £½ bn better than expected for calendar month
12/4

NOTE: this means that the cost of the coal strike accounts for the entire overrun: £10bn – £7¼bn = £2¾bn

PSBR IN MARCH AND IN 1984-85

1. The first provisional outturn for the PSBR in 1984-85 is a little over £10.0 bn, £0.4 bn lower than the Budget forecast of £10.5 bn. This estimate is subject to revision before publication on Thursday 18 April. The estimate for March is £2.5 bn (the market expectations are evenly spread between £2 bn and £3 bn).

2. The CGBR(O) in 1984-85 is £6.6 bn, £0.3 bn lower than the Budget forecast (see table attached). (This difference is slightly smaller than reported in Mr Devereux's note of 2 April, because of new information.) The difference is due to £0.3 bn lower supply expenditure; receipts were as forecast: £0.2 bn higher Customs receipts (probably mostly on VAT) were offset by slightly lower Inland Revenue receipts (largely income tax) and a smaller National Insurance Fund surplus.

3. The LABR in 1984-85 is £2.4 bn, as forecast.

4. The PCBR in 1984-85 is £1.0 bn, £0.2 bn lower than forecast. The difference is largely due to lower borrowing by NCB, because of slippage of back pay to miners out of March into 1985-86, and lower PDC payments to British Steel. (Apart from any revisions before publication next Thursday, the PCBR in particular is subject to further revision when the banks' quarterly returns come in: this could affect the outturn by up to £¼ bn either way.)

5. The monthly note, presenting updated estimates of outturn for 1984-85 and a forecast monthly profile for 1985-86, will be circulated next Wednesday. As usual we shall send you a copy of the draft press briefing at the same time.

MEP

MISS M E PEIRSON

5/28

£ billion

	March 1985			1984-85			1983-84
	Provisional outturn	Last month's forecast	Difference	Provisional outturn	Budget profile	Difference	Outturn*
CGBR(O)	1.5	1.8	- 0.3	6.6	6.8	- 0.3	8.2
LABR	1.1	1.0	-	2.4	2.4	-	1.2
PCBR	- 0.1	0.1	- 0.3	1.0	1.3	- 0.2	0.3
PSBR	2.5	2.9	- 0.5	10.0	10.5	- 0.4	9.7

* New definition

37/6

~~BH~~
~~RR~~
return to me

SECRET

(HB9)

FROM: MS D J SEAMMEN

DATE: 11 April 1985

NOTE OF A MEETING ON 10 APRIL 1985

Para 16.

Those present:
Mr Anson
Mr Kemp
Ms Seammen
Miss Walker
Mrs Holmans
Mr Isaac - I/R
Mr Heppell)
Mr Montagu) DHSS
Mr Wallace)

The meeting discussed the proposals for the compulsory private scheme to replace SERPS.

Coverage

2. DHSS proposed that very low earners should be excluded, probably by reference to the present LEL. This would bring into the scheme substantial numbers of part timers, particularly in the public services. DHSS would consider whether the Green Paper might suggest an exclusion of part timers by reference to a number of qualifying hours. DHSS and superannuation division would produce an estimate of the extra costs to the public service schemes of bringing in part timers.

3. The exclusion by reference to low earnings would operate by reference to average earnings over a year. This would appear to involve cumulation. Inland Revenue stood ready to advise DHSS on how cumulation might work.

4. The period of 6 months during which new employees did not have to be covered might be too short in the light of Government policies generally towards the creation of new jobs (eg unfair dismissal); DHSS would consider whether a longer period would be appropriate.

Administration

5. It was clear that for employees, whether in employer run schemes or personal pensions, the employer would need to be responsible for deducting the employee contribution. Only those not in employment (the self employed on a compulsory basis, the sick and unemployed on a voluntary basis) would make contributions direct to personal pension providers. It was noted that entirely free choice of personal pension provides, as envisaged by DHSS would lead to heavy burdens on employers; at the extreme, each employee might be contributing, at a different rate, to a different institution.

6. A clearing house run by personal pension providers would be essential to the administration of the scheme. It would provide the information on which to enforce both the minimum contributions (for DHSS purposes) and the maximum contributions (for tax relief purposes). DHSS suggested that, although the clearing house had not been welcomed in the personal pensions context, attitudes might be different given the much greater business flowing from compulsory pensions.

7. It followed that the main routes for enforcement would be via the employer and the clearing house. DHSS needed to give further thought to the penalties for non payment. They accepted that non payment would in the end need to be a criminal offence but they hoped that at least in the early years to proceed largely by persuasion.

8. It was agreed that the Green Paper should say much more about administration of the scheme. Subsequently, DHSS said that they had in mind a separate but simultaneous consultation document on the administrative aspects.

Contributions

9. The Treasury said that, since this scheme was designed to avoid dependence on supplementary benefit, DHSS should

be clear whether contributions of 4% or 5% of earnings (or perhaps less) would be sufficient to achieve that objective. Moreover, it was not sensible in that context that compulsory contributions should run right up the income scale; a cut off point of no more than average earnings would seem appropriate. While an increase in employment costs, and reduction in take home pay, was a necessary consequence of a switch to funding, these effects should be minimised so far as possible.

10. DHSS undertook to consider this, and to provide calculations showing what level of contributions would avoid supplementary benefit dependence. They noted however that a further objective of the scheme was to extend the coverage of private and occupational pensions and that they wished to produce the simplest possible scheme.

11. The increase in the contracted out rate following SERPS abolition was a necessary consequence, notwithstanding the substantial incrases in public expenditure on public service schemes which would result; SERPS abolition gave much greater public expenditure savings in long run; DHSS noted that it might be possible to use some of the accumulated NI Fund surplus to cushion the effect on employers and employees by reducing the new, unified, NIC rate from april 1987. This would need to be considered in the light of fiscal prospects nearer the time.

Self employed

12. It was agreed that there was no logical case for excluding the self employed, but obviously this would be highly contentious.

13. The problem of policing arose in an acute form. DHSS envisaged that the Inland Revenue would check the self employed tax returns to ensure that minimum payments had been made. Given the infrequency and unreliability of self-employed tax returns it was accepted that policing would be largely ineffective.

Institutions

14. The Green Paper made clear the distinction between institutions able to act as "money boxes" which would cover a wide range of institutions, and those - essentially the insurance companies - which would provide the pensions on retirement. DHSS would be responsible for approving institutions, qualifying investments etc.

15. The Treasury said that it must be made crystal clear in the Green Paper that, inspite of the compulsory nature of the scheme, the Government took no responsibility for underwriting it. The eventual pension would depend entirely on the performance of the chosen institution. DHSS were considering whether the clearing house might incorporate a protection fund.

X 16. The Treasury in consultation with DHSS, GAD and the Inland Revenue would attempt a long term flow of funds analysis showing flows of funds into the institutions, tax relief etc, in the light of decisions on the appropriate level of contributions.

Benefits

17. DHSS confirmed that those opting for personal pensions would have no facility to take accrued rights from an employers' scheme, although there would be no bar on employers allowing this.

18. On integration, DHSS proposed no change on the present position; there would be neither compulsion nor persuasion on employers to integrate. A brief reference in the Green Paper might be appropriate given the fact that Lord Vinson and Mr Chappell were currently interested in the subject.

19. The main question arising under this heading was indexation of public service pensions. New compulsory schemes would be required to index by the lesser of RPI and 5%. (DHSS

in terms of salary links - not in terms of indexation

later confirmed that, given the superior benefits offered by currently contracted out schemes, there was no intention of applying the new indexation requirement to them.) DHSS confirmed that accrued SERPS rights would at least be price protected, so that the statutory basis for indexing public service pensions would remain.

20. Nonetheless the future of public service index linking would certainly arise on publication of the Green Paper. Mr Kemp would clear with DHSS a paper for Treasury Ministers to put to Cabinet on the same date as Mr Fowler's Green Paper.

Tax

21. Four further points were made

(i) For personal pensions the present retirement annuity maximum would apply; but to the total of employer and employee contributions;

(ii) no tax relief would be available on personal pension contributions if the person were also a member of an employer's scheme;(iii) the compulsory pension could not be commuted into a lump sum; this would be made clear in the Green Paper.

(iv) the clearing house would also need to give information on benefits to the Inland Revenue so that the appropriate PAYE code could be applied where a person had a number of different pensions; such cases would arise much more frequently under the new system.

Conclusions

22. Aside from the commissions itemised throughout, it was agreed

(i) DHSS would send to the Treasury and Inland

Revenue a paper setting out in detail how the administration of the scheme would work. This would be a basis for calculating staff implications in DHSS, Inland Revenue and departments administering public service schemes; ST1 would co-ordinate estimates from DHSS, IR and superannuation division;

(ii) the calculations on contribution rates attached to Mr Fowler's minute would be reworked (this is now in train between Treasury, GAD and DHSS;

(iii) Treasury would send DHSS notes on the macro-economic implications of the compulsory scheme (now done, in agreement with Mr Odling-Smee).

23. It was not presently envisaged that the whole of the Green Paper would go to Cabinet. DHSS would send a draft of their Secretary of State's paper. The Treasury said that it should bring out the most sensitive points - eg the effect on employment costs, the appropriate level of contributions, the position of the self employed, macro-economic aspects. It was confirmed that Cabinet was now set for 25 April. DHSS noted the high degree of confidentiality attaching to the proposals; superannuation division would bear this in mind in their consultations.

MS D J SEAMMEN

Copied to:

Those present
Sir P Middleton
Sir T Burns
Mr Monck
Mr Byatt
Mr Odling-Smee
Mr Monger
Mr Lankester
Mr Watson - O/R
Miss Noble

FROM: MISS M E PEIRSON
DATE: 17 April 1985

1. MR ~~CASSELL~~ seen in draft.

2. CHANCELLOR OF THE EXCHEQUER

Copy attached for:

Mr Turnbull - No 10

cc List A	List B (distributed at 2.30 pm, 18 April)	
Sir P Middleton	Chief Secretary	Mr Peretz
Sir T Burns	Financial Secretary	Mr Mowl
Mr H Evans	Economic Secretary	Mr Stibbard
Mr Battishill	Minister of State	Mr M Williams
Mr Lankester	Mr Bailey	Mr Powell
Mr Collinson	Mr Odling-Smee	Mr Cropper
Mr Devereux	Mr Scholar	Mr Wells - CSO
Dr Webb	Mr Burgner	Mr Walton - IR
	Mr Folger	Mr Wilmott - C & E

MONTHLY NOTE ON THE PSBR

1. I attach a report on the PSBR outturn for 1984-85. This outturn will be published by press notice at 2.30 pm tomorrow, Thursday 18 April.

2. In addition to comparisons with the 1985 Budget forecast for 1984-85, this note contains forecast monthly profiles for the PSBR and its components for 1985-86, together with more detailed forecasts for the next three months. The press notice is confined to comparisons between outturn in 1984-85 with outturn in 1983-84.

MEP

MISS M E PEIRSON

PUBLIC SECTOR BORROWING

Summary

- The PSBR for 1984-85 is provisionally estimated at £10.1 billion, about £0.4 billion lower than last month's Budget forecast. The undershoot was equally split between central government own account and public corporations' borrowing.

- The outturn was £0.4 billion higher than the 1983-84 outturn and £2.9 billion above the 1984 Budget forecast (Charts 1 and 2).

- Borrowing is likely to be high in the next three months, though lower than in the same period of 1984-85.

- Monthly borrowing profiles for 1985-86 are presented in this note (Chart 2 and Table 4), together with more detailed forecasts of borrowing for the period April-June.

Figures in this report are not seasonally adjusted and also may not sum precisely because of rounding.

Chart 1 : Comparisons with 1984 Budget profiles for 1984-85

£ billion cumulative

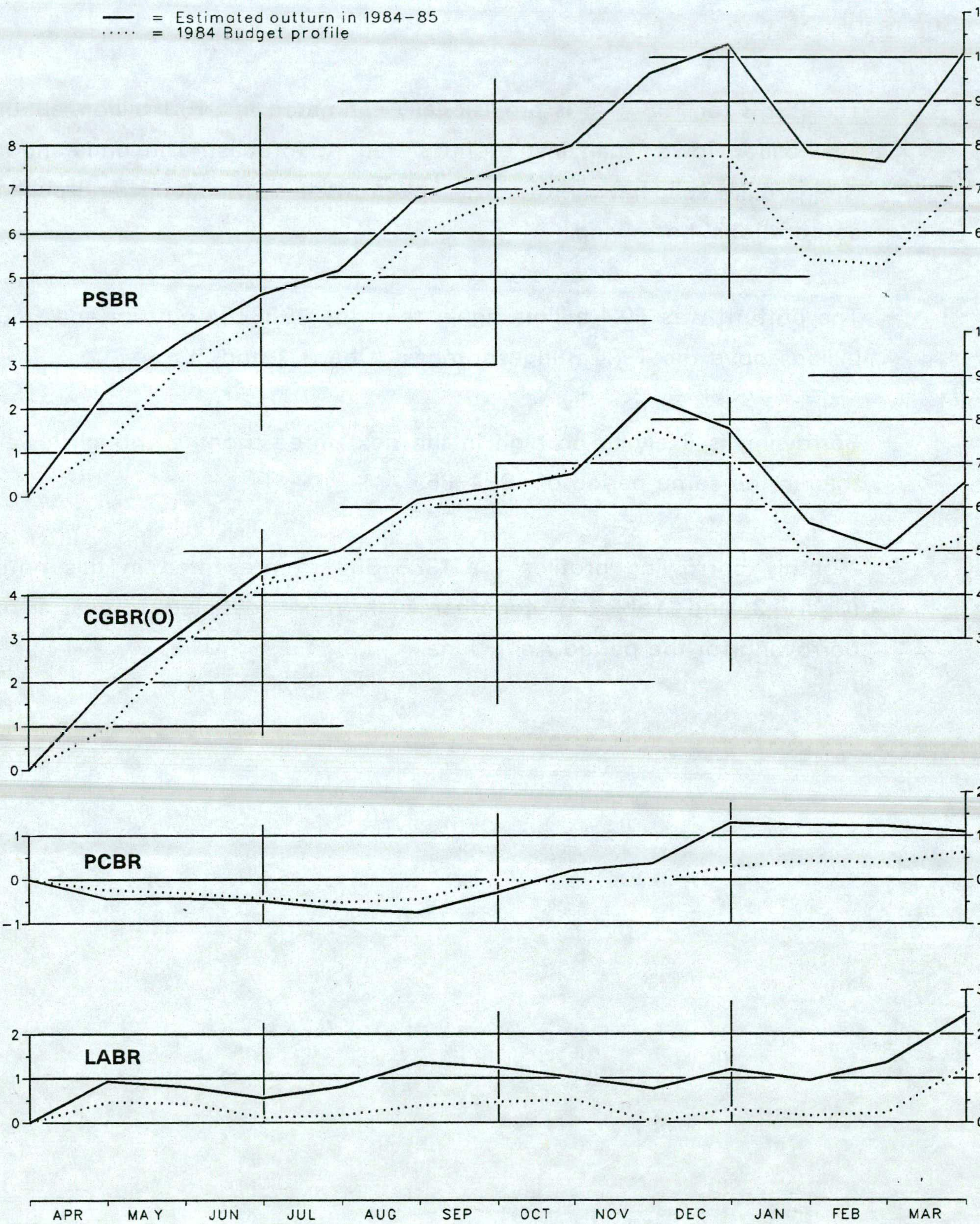
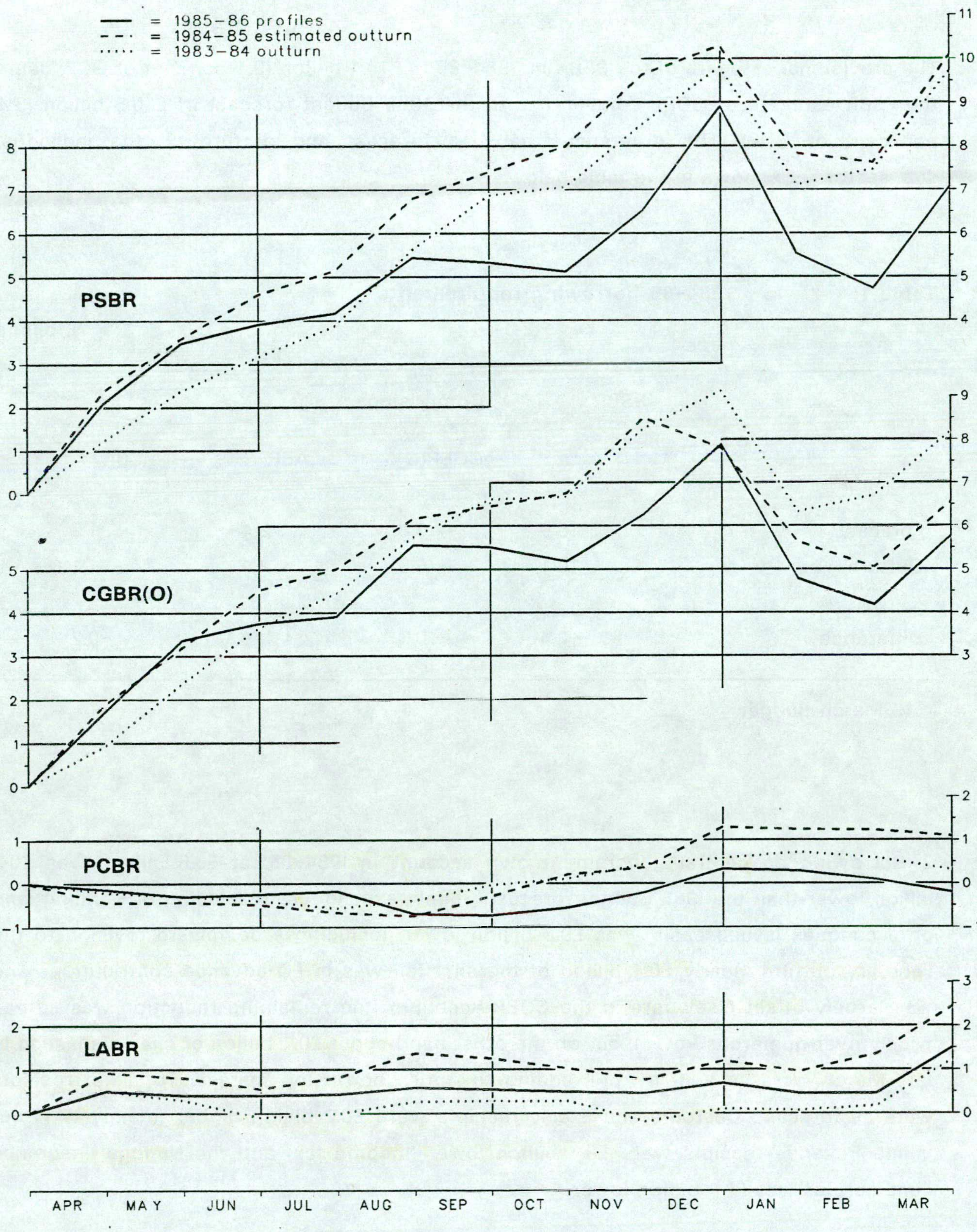


Chart 2 : 1985-86 profiles and outturns for 1983-84 and 1984-85

£ billion cumulative



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Borrowing in 1984-85

(Comparisons in this section are with last month's Budget forecast)

The provisional estimate of the PSBR in 1984-85 is £10.1 billion (3.1 per cent of GDP, using the FSBR estimate of GDP), compared with the 1985 Budget forecast of £10.5 billion (3¼ per cent of GDP). The differences between forecast and outturn on the individual sub-sectors are shown in the table below.

Table 1: 1984-85 borrowing requirements

£ billion

	PSBR	Comprising		
		CGBR(O)	LABR	PCBR
Forecast*	10.5	6.8	2.4	1.3
Outturn	10.1	6.6	2.4	1.1
Difference	-0.4	-0.3	-	-0.2

*19 March Budget

2. Borrowing on central government own account in 1984-85, at £6.6 billion, was £0.3 billion lower than the 1985 Budget forecast. Supply expenditure (excluding on-lending, and on a cheques issued basis) was £0.3 billion lower, including a downward revision to the February outturn: nearly £0.1 billion of the shortfall was in EC advance contributions and was largely offset elsewhere in the CGBR accounts (the remaining reduction was spread widely over numerous votes), but on the other hand about £0.1 billion of cheques issued in late March were cashed in April, adding to April's borrowing instead. Total net receipts were as forecast: Customs and Excise receipts were £0.2 billion higher (mainly VAT) but Inland Revenue receipts were £0.1 billion lower (income tax) and the National Insurance Fund surplus was £0.1 billion lower.

3. The CGBR(0) in March was £1.5 billion. The high figure reflects, as forecast, high supply expenditure.

4. Local authorities borrowed £2.4 billion in 1984-85, as forecast in the 1985 Budget. This includes borrowing of £1.1 billion in March, when no rate income was received and borrowing tends to be high.

5. Public corporations borrowed £1.1 billion in 1984-85, £0.2 billion lower than the 1985 Budget forecast. The main reasons for the shortfall in March are lower than expected borrowing by the NCB reflecting slippage of back pay to miners into 1985-86, and lower PDC payments to BSC.

1985-86

6. The PSBR for 1985-86 was forecast in the 1985 Budget to be £7.1 billion, comprising borrowing of £5.8 billion on central government's own account, £1.5 billion by local authorities and a surplus of £0.2 billion by public corporations.

compared with forecast front-end loading 93% this time last year

7. As in previous years, most of the borrowing is expected in the first half-year (details are shown in Chart 2 and Table 4). For 1985-86, the forecast proportion is 75 per cent, compared with an average of 67 per cent in the 7 years up to and including 1984-85, and 73½ per cent in 1984-85 itself. The forecast degree of front-end-loading in 1985-86 is however very uncertain and depends in particular on the timing of major asset sales (see paragraph 17 below).

8. The main reason why high front-end-loading continues is that Inland Revenue receipts remain concentrated (57 per cent) in the second half of the year. PRT receipts are expected to be a little higher in the first half of 1985-86 (see paragraph 13 below), but 77 per cent (£7.8 billion) of corporation tax receipts are expected to come in the second half, with two large peaks in October and January. The skewness of corporation tax receipts has increased recently, adding to the front-end-loading of the PSBR: the chief reason is the increase in in company profits, leading for example to a forecast £2 billion increase in corporation tax in 1985-86 over 1984-85 (and further increases forecast for later years, though flattening out as the recovery consolidates). Another smaller factor is the abolition

of the National Insurance Surcharge, which has had the effect of partially replacing an evenly-distributed tax by additional (skewed) corporation tax.

9. Customs receipts are also forecast a little higher (52 per cent) in the second half of 1985-86. This concentration of Revenue and Customs receipts is only partially offset by supply expenditure's also being forecast a little higher in the second half (51½ per cent) and by most asset sales being forecast to come in the first half.

10. By contrast, the bulk of asset sales in 1984-85 came in the second half, which also benefitted from the change in VAT on imports. Therefore, much higher front-end-loading than usual was expected in that year, until the costs of the coal strike began to appear, adding to borrowing in the second half.

11. The major differences in particular months between the profiles for 1984-85 and 1985-86 shown in Chart 2 arise for the following main reasons:

- (i) lower borrowing in June 1985 than in June 1984 because of the BT second call receipts;

- (ii) lower borrowing in September 1985 than in September 1984 because of the higher PRT peak (see paragraph 13(a) below) and a higher PCBR (public corporations' borrowing in September 1984 began to rise, probably affected by the coal striko);

- (iii) lower borrowing in October 1985 than in October 1984 because of higher corporation tax (see paragraph 13(c) below) and a lower PCBR;

- (iv) higher borrowing in December 1985 than in December 1984 because the latter was reduced by the BT first call receipts and the change in VAT on imports;

- (v) lower borrowing in January 1986 than in January 1985, despite the effect on the latter of the change in VAT on imports, because of higher corporation tax (see below);

- (vi) lower borrowing in February 1986 than in February 1985 mainly because of a lower LABR (though that is clearly uncertain).

CGBR(0)

12. The main feature of the profile for borrowing on central government's own account is the high level of borrowing forecast for the first five months of the year (over £5½ billion, nearly the same as the total borrowing forecast for 1985-86), repeating the significant front-end-loading recorded in 1984-85. It is expected that this will be followed by forecast borrowing of nearly £2½ billion in the December quarter and a net repayment of £2 billion in the final quarter. Notes on the profiles for the main items of the account are as follows.

Inland Revenue

13. In general, the main categories of tax receipts are likely to follow the pattern recorded in 1984-85. January will see the peaking of both Income tax and Corporation tax receipts (expected to total nearly £9 billion) while other favourable months can be expected in July (high Advanced Corporation Tax and Schedule D receipts); September (peaking of PRT receipts); October (high Mainstream Corporation tax receipts); February (high Schedule D receipts) and March (high PRT receipts). A number of special factors affecting 1985-86 have also been taken into account, viz:-

- (a) PRT receipts will peak in September (£2¼ billion) and March (£1 billion). The September peak is £¾ billion higher than in September 1984 but the March peak is £¾ billion lower than in March 1985. Part of the PRT payment in September 1985 makes good the difference between liabilities in January-June 1985 and earlier payments on account based on liabilities in July-December 1984. As the Budget forecast included rises in the £ oil price (based on the forecast pound:dollar exchange rate) and in oil production between July-December 1984 and January-June 1985, the settling-up part of the September 1985 payment is relatively large. On the other hand the Budget forecast included a fall in the £ oil price between January-June 1985 and July-December 1985 with the result that the settling-up part of the March 1986 payment is negative, producing a relatively small peak.

- (b) Introduction of the bank composite rate tax (tax deducted at source on interest on individuals' bank deposits) will lead to increased Income tax receipts in July, October and January when the banks pay over these taxes. These will be offset by reductions in other months.

- (c) Corporation tax in October will be relatively higher in 1985 than in 1984, reflecting increased receipts expected from oil companies, higher Advance Corporation Tax receipts, and the first payments of Mainstream Tax on the relatively high 1984 profits.

- (d) Corporation tax in January 1986 will also be relatively higher than in January 1985, reflecting the relatively high 1984 profits.

Customs and Excise

14. There are three major changes compared with 1984-85. First, the change in arrangements for payment of VAT on imports produced a large "once and for all" benefit in the last 4 months of 1984-85. Secondly, the introduction from 15 October 1985 of duty deferment arrangements for the payment of duties on hydrocarbons means that half the hydrocarbon duties due in October (worth £¼ billion) will slip into November. Thirdly, VAT receipts in April 1985 are expected to be £½ billion higher than in April 1984; the slightly later date of the 1985 Budget meant that some of the duty on tobacco, wines etc usually received in March slipped into April. Apart from these factors, the pattern of total receipts largely follows the usual incidence of the payment of VAT receipts, where traders are grouped into three quarterly payment cycles, the most favourable being the May/August/November /February cycle.

Supply expenditure

15. Supply expenditure (excluding on-lending) is forecast to be slightly lower (48½ per cent) in the first half of 1985-86 than in the second. This is markedly higher than in 1984-85 (47 per cent), when expenditure in the second half was increased by the coal strike, and by EC advance payments (see below).

16. Particular features of the forecast profile for 1985-86 are as follows:

(a) Cash limited items

These are expected to follow a similar pattern to the out-turns in previous years, including the usual "end-year" surge in March.

(b) Non-cash-limited items

Student awards, teachers' superannuation and rate rebate payments are assumed to exhibit their "normal" lumpiness of expenditure. Agricultural support payments are also rather variable, though the pattern is particularly uncertain. There will be a number of special factors affecting 1985-86, as follows:-

- (i) The forecast assumes that EC advanced contributions will be required (at the rate of £120 million per month) for each month of 1985-86 except September and December. However, these payments offset those normally paid out of standing services and so should not affect the CGBR(0) over the year as a whole. In 1984-85, similar EC advanced contributions were required only in the second half of the year.

- (ii) The high August figure reflects expected grants to NCB totalling £¾ billion, in settlement of the 1984-85 coal strike costs (offset in the PCBR - see below).

- (iii) The forecast for December includes £200 million for a payment to the ROFs' pension fund.

- (iv) Net ECGD receipts are expected in January, covering expected refinancing of existing Brazilian and Yugoslavian debt.

Special sales of assets

17. The 1985 Budget forecast of total asset sales in 1985-86 is £2.5 billion, compared with the outturn of £2.1 billion in 1984-85. There are major uncertainties, particularly as regards the timing of receipts. The forecast profile differs markedly from that in 1984-85. In particular, the BT first call of £1.3 billion was received in December 1984 whilst the BT second call of £1.2 billion is due in June 1985 (though some of these receipts are assumed to slip into July).

Other items

18. Items of note are the following:-

- (i) The profile for the National Insurance Fund depends on the flows of income and expenditure into and out of the Fund, which are very large (around £2 billion in each direction each month), and the margin of error is considerable. The present forecast displays a similar pattern to that recorded in 1984-85; in particular a large deficit of £0.4 billion in December partially offset by a large surplus of £0.3 billion in January. The forecast takes account of the changes in National Insurance contributions announced in the Budget, which are expected to reduce income by £0.2 billion in 1985-86.

- (ii) Interest and dividend receipts will be boosted in 1985-86 by share dividends on BT ordinary shares forecast to be £170 million in August and £120 million in February.

- (iii) Gross contributions to the EC are expected to peak in August (at around £300 million) on the assumption that the EC Budget is agreed by Member States in June/July; a similar peak is expected in March 1986 to coincide with the assumed payment to the UK in that month of the EC negotiated refund in respect of 1984 (£0.6 billion). The "refund" in respect of 1985 will be effected by a reduction (abatement) of contributions in 1986. It has been assumed that these abatements will begin in March 1986 (with an abatement covering January-March of £0.2

billion) with monthly abatements thereafter.

- (iv) Receipts from the National Insurance Surcharge in the first eight months of 1985-86 will be only £30 million, compared with £¾ billion in the same months of 1984-85, because the surcharge has been phased out.

- (v) The profile for service of the National Debt is similar to 1984-85, with large payments in May, July, November and January.

- (vi) The item "Other Central Government Funds and Accounts" is forecast to add substantially to borrowing in 1985-86 compared with 1984-85 (see Table 6). However, this difference mostly reflects various adjustments in 1984-85 which were offset elsewhere in the accounts and so had no effect on the CGBR(O), and which are not forecast for 1985-86. (That is, the underlying position in 1984-85 was, as in 1985-86, a large addition to borrowing, reflecting national savings accrued interest.)

LABR

19. The profile for local authorities' borrowing in 1985-86 (Chart 2 and Table 4) is estimated by deriving seasonal factors from borrowing patterns of previous years, together with allowance for a special factor operating in 1985-86: from 1 April 1985, non-domestic ratepayers of any size are entitled to pay rates by monthly instalments, rather than annually or semi-annually. Borrowing in June and November, historically low, has consequently been forecast higher than in the past, and borrowing in other months reduced. A major feature of the profile, reflecting historical patterns, is heavy borrowing in April 1985 and March 1986, the months of little or no rate income. (The borrowing pattern in 1984-85 was more than usually erratic, probably partly reflecting anticipation of the new capital controls system.)

PCBR

20. Public corporations are expected to show a net repayment of debt in the first half of 1985-86, with seasonally high borrowing in the December quarter and repayments in early 1986. The profile is derived mainly from the limited information currently available from individual industries. The unusually large repayment of £½ billion forecast for August arises from an expected grant of £¾ billion to the National Coal Board in the month (see 16(b)(ii) above). Borrowing is expected to be lower in the latter part of 1985-86 compared with the same period last year, which was affected by the coal strike.

April to June

21. Borrowing is likely to be high in the next three months, though slightly lower than in the same months of 1984-85.

22. Borrowing on central government's own account in April to June is forecast to be around £3¾ billion, about £¾ billion lower than in the same period last year (because of the BT second call in June).

23. Following seasonally high borrowing in April, when little rate income is received, local authorities are expected to show small net repayments of debt in May and June. Public corporations are likely to be in surplus over the first quarter of 1985-86, with the Electricity Supply Industry and British Gas Council showing large repayments of debt.

Table 2: 1984-85: Outturns

£ billion

	PSBR	Comprising		
		CGBR(O)	LABR	PCBR
1984-85				
Apr	2.4	1.9	0.9	-0.4
May	1.2	1.3	-0.1	-
Jun	1.0	1.3	-0.3	-0.1
Jul	0.6	0.5	0.3	-0.2
Aug	1.6	1.2	0.6	-0.1
Sep	0.6	0.3	-0.1	0.5
Oct	0.6	0.3	-0.2	0.5
Nov	1.6	1.7	-0.3	0.2
Dec	0.7	-0.7	0.4	0.9
Jan	-2.5	-2.2	-0.2	-0.1
Feb	-0.2	-0.6	0.4	-
Mar	2.5	1.5	1.1	-0.1
Cumulative				
Apr	2.4	1.9	0.9	-0.4
May	3.6	3.2	0.8	-0.4
Jun	4.6	4.5	0.6	-0.5
Jul	5.2	5.0	0.8	-0.7
Aug	6.8	6.2	1.4	-0.7
Sep	7.4	6.4	1.2	-0.3
Oct	8.0	6.8	1.0	0.2
Nov	9.6	8.5	0.8	0.4
Dec	10.3	7.8	1.2	1.3
Jan	7.8	5.6	1.0	1.2
Feb	7.6	5.0	1.4	1.2
Mar	10.1	6.6	2.4	1.1

Table 3: PSBR for 1984-85 – Comparisons with 1983-84 and Budget profile

£ billion

	1983-84	1984-85		Differences from	
	Outturn	1984 Budget profile	Latest update	1983-84 outturn	1984 Budget profile
	1	2	3	3-1	3-2
Apr	1.2	1.2	**2.4**	1.1	1.2
May	1.1	1.9	**1.2**	0.1	-0.7
Jun	0.8	0.9	**1.0**	0.2	0.1
Q2	3.2	3.9	**4.6**	1.4	0.7
Jul	0.7	0.3	**0.6**	-0.2	0.3
Aug	1.7	1.8	**1.6**	-0.1	-0.1
Sep	1.2	0.8	**0.6**	-0.6	-0.2
Q3	3.7	2.8	**2.8**	-0.9	-
Oct	0.2	0.6	**0.6**	0.4	-
Nov	1.4	0.5	**1.6**	0.2	1.2
Dec	1.3	-	**0.7**	-0.6	0.7
Q4	2.9	1.0	**2.9**	-0.1	1.9
Jan	-2.7	-2.3	**-2.5**	0.2	-0.1
Feb	0.4	-0.1	**-0.2**	-0.6	-0.1
Mar	2.3	1.9	**2.5**	0.2	0.6
Q1	-0.1	-0.5	**-0.2**	-0.1	0.3
Cumulative					
Apr	1.2	1.2	**2.4**	1.1	1.2
May	2.4	3.0	**3.6**	1.2	0.6
Jun	3.2	3.9	**4.6**	1.4	0.7
Jul	3.9	4.2	**5.2**	1.3	1.0
Aug	5.6	6.0	**6.8**	1.2	0.8
Sep	6.9	6.7	**7.4**	0.5	0.7
Oct	7.1	7.3	**8.0**	0.9	0.7
Nov	8.5	7.8	**9.6**	1.1	1.8
Dec	9.8	7.7	**10.3**	0.5	2.5
Jan	7.1	5.4	**7.8**	0.7	2.4
Feb	7.5	5.3	**7.6**	0.2	2.3
Mar	9.7	7.2	**10.1**	0.4	2.9

Table 4: **Borrowing requirement monthly profiles 1985-86**

£ billion

		PSBR	Comprising CGBR(O)	LABR	PCBR
1985-86					
Apr		2.1	1.7	0.5	-0.1
May		1.4	1.6	-0.1	-0.2
Jun		0.4	0.4	–	0.1
Jul		0.3	0.2	–	0.1
Aug		1.3	1.6	0.2	-0.5
Sep		-0.1	–	–	–
Oct		-0.2	-0.3	-0.1	0.2
Nov		1.4	1.1	–	0.4
Dec		2.4	1.6	0.2	0.5
Jan		-3.4	-3.1	-0.2	–
Feb		-0.8	-0.6	–	-0.2
Mar		2.3	1.6	1.0	-0.3
Cumulative					
Apr		2.1	1.7	0.5	-0.1
May	3.9	3.5	3.4	0.4	-0.3
Jun		3.9	3.8	0.4	-0.2
Jul		4.2	3.9	0.4	-0.2
Aug	1.4	5.4	5.6	0.6	-0.7
Sep		5.3	5.5	0.5	-0.7
Oct		5.1	5.2	0.5	-0.6
Nov	3.6	6.5	6.3	0.5	-0.2
Dec		8.9	7.9	0.7	0.3
Jan		5.5	4.8	0.5	0.3
Feb	-1.8!	4.7	4.2	0.5	0.1
Mar		7.1	5.8	1.5	-0.2

Table 5: Central government transactions – March outturn and latest forecasts for April–June

£ billion

	March		Latest forecasts		
	forecast	outturn(1)	Apr	May	Jun
Receipts					
Consolidated Fund					
Inland Revenue	5.2	5.1	3.7	3.7	3.1
Customs and Excise	2.7	2.9	3.1	2.8	2.0
Other(2)	1.8	1.5	0.6	1.2	1.8
National Loans Fund					
Interest etc. receipts	0.8	0.8	0.5	0.5	0.6
Total Receipts	10.5	10.2	8.0	8.1	8.1
Expenditure					
Consolidated Fund					
Supply expenditure(3)	10.3	10.4	8.3	7.7	7.6
Adjustment to Supply Services basis(4)	–0.3	–0.7	–	–	–
Other	0.3	0.4	0.3	0.3	0.3
National Loans Fund					
Service of the national debt	1.0	1.0	1.0	1.5	0.5
Net lending	–	0.1	0.1	0.3	0.2
Total Expenditure	11.3	11.2	9.6	9.8	8.7
Other funds and accounts (+ increases borrowing) (– reduces borrowing)	1.5	1.3	0.2	0.2	0.1
CGBR	**2.4**	**2.3**	**1.9**	**1.9**	**0.7**
On-lending	0.6	0.7	0.1	0.3	0.3
CGBR(O)	**1.8**	**1.5**	**1.7**	**1.6**	**0.4**

(1)Due to time lags in some items reaching their final accounting destination, figures of forecast and outturn may not be strictly comparable for the components identified, but there is no effect on the overall CGBR.
(2)Includes National Insurance Surcharge and receipts from sales of assets
(3)On a cheques issued basis. Supply includes an element of on-lending in the form of public dividend capital etc.
(4)Reflects changes in balances of departmental accounts with the Paymaster General, timing and other differences between cheques issued by departments and payments to them from the Consolidated Fund. An offset to this item is included in "Other funds and accounts".

Table 6: Central government transactions[1] – comparisons for the full financial year

£ billion

	1984-85		1985-86
	1985 Budget forecast	Outturn	1985 Budget forecast
Receipts			
Consolidated Fund			
Inland Revenue	50.5	50.4	56.2
Customs and Excise	35.3	35.5	36.4
Other[2]	12.6	12.4	13.9
National Loans Fund			
Interest etc. receipts	5.4	5.4	6.4
Total Receipts	103.9	103.7	112.9
Expenditure			
Consolidated Fund			
Supply expenditure[3]	93.8	93.4	99.6
Adjustment to Supply Services basis[4]	–	–	–
Other	4.5	4.6	4.4
National Loans Fund			
Service of the national debt	12.9	12.9	14.1
Net lending	2.4	2.5	2.4
Total Expenditure	113.6	113.5	120.5
Other funds and accounts (+ increases borrowing) (- reduces borrowing)	0.4	0.2	1.5
CGBR	**10.1**	**10.0**	**9.0**
On-lending	3.3	3.5	3.3
CGBR(O)	**6.8**	**6.5**	**5.8**

[1]Due to differences in treatment of some items in the accounts between the periods/forecasts shown, and time lags in some items reaching their final accounting destination, figures for the components identified may not be strictly comparable.
[2]Includes National Insurance Surcharge and receipts from sales of assets.
[3]On a cheques issued basis. Supply includes an element of on-lending in the form of public dividend capital etc.
[4]Reflects changes in balances of departmental accounts with the Paymaster General, timing and other differences between cheques issued by departments and payments to them from the Consolidated Fund. An offset to this item is included in "Other funds and accounts".

COVERING CONFIDENTIAL & PERSONAL

FROM: MISS M E PEIRSON
DATE: 17 April 1985

PPS/CHANCELLOR

cc Mr Cassell

MONTHLY NOTE ON PUBLIC SECTOR BORROWING, AND PRESS BRIEFING

1. Later today I will send the latest monthly note on the PSBR to the Chancellor. As usual, it will be accompanied by an additional copy for you to forward to No 10.

2. A draft covering letter for you to send to Andrew Turnbull is attached. The note should reach No 10 this evening.

3. In the Chancellor's absence we shall not trouble you with the draft press briefing. We shall circulate the briefing tomorrow.

MEP

MISS M E PEIRSON

COVERING CONFIDENTIAL & PERSONAL

pmp

From: JOHN CLARK
18 April 1985

MR CULPIN - IDT

MR LANG - CSO Press Office

cc List A

Chancellor
Sir P Middleton
Sir T Burns
Mr Cassell
Mr H Evans
Mr Lankester
Mr Collinson
Mr Folger
Miss Peirson
Mr Peretz
Mr R Evans
Mr Ward - CSO
Mr Wright - Bank of England
Mr Turnbull - No. 10

List B (distributed at 2.30pm, 18 April)

Chief Secretary
Financial Secretary
Economic Secretary
Minister of State
Mr Stibbard
Mr Spencer
Mr Cropper
Mr Lord
Mrs Hillier - Inland Revenue
Mr D Mitchell - Customs and Excise

BRIEFING FOR 18 APRIL PSBR PRESS NOTICE

The PSBR figures for March will be published at 2.30pm on 18 April. The provisional outturns, together with 1983-84 figures, are shown in Table 1. Cumulative figures for the PSBR and its components for 1983-84 and 1982-83 are shown in Table 2 overleaf.

Table 1: Borrowing requirement outturns

£ billion

	1983-84	1984-85	March 1985
Central government on own account	8.2	6.6	**1.5**
Local authorities	1.2	2.4	**1.1**
Public corporations	0.3	1.1	**-0.1**
PSBR	9.7	10.1	**2.5**
Memo: CGBR (including borrowing for on-lending to LAs and PCs)	12.3	10.0	**2.3**

Note: All figures are on the new definition. Figures may not sum precisely because of rounding.

Table 2: PUBLIC SECTOR BORROWING REQUIREMENT – Comparison with the last two years

Cumulative £ billion

	Central government on own account			Local authorities borrowing requirement			Public corporations borrowing requirement			Public sector borrowing requirement		
	1982–83	1983–84	1984–85	1982–83	1983–84	1984–85	1982–83	1983–84	1984–85	1982–83	1983–84	1984–85
Apr	1.0	0.9	**1.9**	0.3	0.5	**0.9**	–0.6	–0.2	**–0.4**	0.8	1.2	**2.4**
May	2.3	2.4	**3.2**	0.2	0.3	**0.8**	–0.6	–0.3	**–0.4**	1.8	2.4	**3.6**
Jun	3.3	3.7	**4.5**	–0.3	–0.1	**0.6**	–0.3	–0.4	**–0.5**	2.7	3.2	**4.6**
Jul	3.6	4.5	**5.0**	–0.3	–0.0	**0.8**	–0.2	–0.6	**–0.7**	3.1	3.9	**5.2**
Aug	4.6	5.7	**6.2**	–0.3	0.3	**1.4**	–0.2	–0.4	**–0.7**	4.2	5.6	**6.8**
Sep	4.2	6.6	**6.4**	–0.4	0.3	**1.2**	0.5	–0.0	**–0.3**	4.4	6.9	**7.4**
Oct	4.4	6.7	**6.8**	–0.4	0.3	**1.0**	0.7	0.1	**0.2**	4.6	7.1	**8.0**
Nov	5.7	8.3	**8.5**	–1.0	–0.2	**0.8**	0.8	0.4	**0.4**	5.5	8.5	**9.6**
Dec	7.2	9.1	**7.8**	–1.0	0.1	**1.2**	0.9	0.6	**1.3**	7.1	9.8	**10.3**
Jan	5.2	6.3	**5.6**	–1.2	0.1	**1.0**	1.0	0.7	**1.2**	5.1	7.1	**7.8**
Feb	5.8	6.7	**5.0**	–1.1	0.2	**1.4**	1.2	0.6	**1.2**	6.0	7.5	**7.6**
Mar	7.2	8.2	**6.6**	0.1	1.2	**2.4**	1.5	0.3	**1.1**	8.9	9.7	**10.1**

Note: All figures are on the new definition. Figures may not sum precisely because of rounding.

CONFIDENTIAL AND PERSONAL
(until 2.30pm 18 April 1985)

2. The (provisional) PSBR for March is £2.5 billion, bringing the total for 1984-85 to £10.1 billion. This is in line with forecasts of City analysts, which are for borrowing of between £2 billion and £3 billion in March, with an average of about £2½ billion.

3. The 1984-85 outturn is £0.4 billion below the 1985 Budget forecast of £10.5 billion, and £0.4 billion higher than outturn for 1983-84 (Table 2). It is £2.9 billion higher than the 1984 Budget forecast of £7.2 billion for 1984-85.

4. The Q and A briefing below gives background and sets out the line to take on particular issues. Comparisons are between 1984-85 and 1983-84.

Q1. Why is 1984-85 outturn lower than expected ?

Background

The PSBR for 1984-85 was forecast to be £10½ billion in the 1985 Budget. An undershoot of about £¼ billion was recorded on each of central government own-account and public corporations' borrowing.

Line to take

The estimated outturn is well within the average margin of error of £1 billion on PSBR forecasts for the current year made in the Budget. Estimate is still only provisional. The undershoot of nearly £½ billion was split equally between central government's own account and public corporations. The central government undershoot was on expenditure; the public corporations undershoot was partly because of delay by the Coal Board in paying back pay to miners (see Q11). Local authority borrowing was as expected. (Miners' strike, £2¾ billion, accounts for almost whole of overshoot on 1984 Budget forecast.)

Q2. What was 1984-85 PSBR as a percentage of GDP?

Line to take

3.1 per cent of GDP, using 1985 FSBR estimate of GDP, compared with 1985 Budget forecast of 3¼ per cent.

Q3. Effect of miners' strike on PSBR in 1984-85 ?

Line to take

In his Budget speech the Chancellor gave the estimated effect of the coal strike on the 1984-85 PSBR as £2¾ billion. The (slightly revised) outturn for 1984-85 PSBR does not affect that estimate significantly. (Delay in back pay to miners may have reduced it slightly.)

Q4. Total public spending in 1984-85?

Background

An estimate of the public expenditure planning total for 1984-85 of £129.7 billion was shown in the 1985 FSBR, nearly £3½ billion higher than forecast a year ago.

Line to take

First indications of outturn from Supply Issues data (see Q5) suggest that public expenditure may have been slightly less than estimated in the FSBR, but there are still substantial uncertainties which could go either way. E.g. it will be some months before reasonably firm local authority figures are available. The first provisional outturn for the planning total as a whole is due to be published in the June issue of Financial Statistics.

Q5. Accuracy of supply expenditure estimate for 1984-85 in FSBR?

Background

1985 FSBR Table 5.3 showed a forecast for total supply of £93.8 billion (planning total element £70.6 billion). Provisional outturn is £93.4 billion (planning total element £70.4 billion).

Line to take

Spending in March was slightly lower (£0.3 billion) than expected in early March, when Budget 'estimated outturn' was compiled. Only about two thirds of this relatively small undershoot contributed directly to the planning total.

Q6. High rate of increase in supply spending over 1983-84?

Line to take

The increase in Supply services over 1983-84 is 7.7 per cent. The coal strike had a major effect on supply expenditure in 1984-85. Excluding three votes severely affected by the strike [NCB grants, lending to British Steel and grants for police pay], the increase is about 6½ per cent. Take-up of social security benefits continued to increase rapidly in 1984-85, and outturn on pension and supplementary benefits are both expected to be 13 per cent higher in 1984-85 than in 1983-84.

Q7. What is the position on EC refunds?

Line to take

European Parliament has released 1983 refund The final £44 million was paid at the end of March, bringing the total to £588 million. 1984 refund expected in 1985-86. 1985 arrangements are different, and will reduce UK monthly contributions, starting in 1986.

Q8. Inland Revenue receipts in 1984-85?

Line to take

Inland Revenue receipts for 1984-85 were £50,350 million, some £150 million lower than the 1984 and 1985 Budget forecasts (both £50,500 million), due to slightly lower than expected income tax payments in the latter half of March.

Compared with the 1984 Budget forecast, oil tax receipts in 1984-85 were some £1200 million higher and non-oil tax receipts were some £1,350 million lower. Most of the latter shortfall is due to income tax; the major factors were the coal strike, lower than expected receipts from the self employed, and higher than forecast repayments to exempt institutions, such as pension funds.

Q9. Customs and Excise revenues?

Line to take

Outturn in 1984-85 at £35,500 million very close to 1985 Budget forecast of £35,300 million and 1984 Budget forecast of £35,000 million. The 1984 forecast included £1¼ billion for changed accounting for VAT on imports: effect now put at £1½ billion.

Q10. Local authorities' borrowing?

Background

Preliminary estimate is that local authorities borrowed £1.1 billion in March, bringing the total borrowing in 1984-85 to £2.4 billion, as forecast in 1985 FSBR. Main reason why 1984-85 borrowing is higher than 1984 FSBR figure (£1.3 billion) is overspending by local authorities on capital expenditure. A second, but relatively minor, reason is the spill over from 1983-84 into 1984-85 of borrowing associated with high payments of home improvement grants in March 1984.

Line to take

Main reason for overshoot on 1984 FSBR forecast is high local authority capital spending. 1985 FSBR forecast remarkably accurate.

Q11. Why has the PCBR undershot 1985 Budget forecast?

Background

Provisional outturn for 1984-85 is £1.1 billion, compared with forecast of £1.3 billion in 1985 FSBR (and £0.6 billion in 1984 FSBR).

Line to take

Undershoot quite small taking into account large flows involved, and figures may be revised when more comprehensive information comes in. Part of undershoot seems to be slippage of miners' back pay into 1985-86. (Overshoot compared with 1984 Budget forecast is owing to coal strike.)

Q12. Does this slippage of miners' pay mean higher PSBR for 1985-86?

Line to take

Probably not. The slippage will be taken into account in reviewing NCB's EFL (PEWP figure was stated as provisional), but any increase would have to be met from the £5 billion Reserve.

Q13. When will outturn, in detail of Table 6.5 of FSBR, be published?

Line to take

In June Financial Statistics.

Q14. Why large fall in OCGFA in March?

Background

This is a detail of government accounting. A major item within OCGFA is changes in the balances on departmental accounts with the Paymaster General. Departmental balances are affected by timing differences between Supply Issues from the Consolidated Fund and actual departmental expenditure. Departmental balances are similarly affected by timing differences with their receipts, which are ultimately paid into the Consolidated Fund. Large fluctuations in OCGFA are not uncommon – for example December 1982, March 1983 and October 1984.

Line to take

The large fall in OCGFA in March is due mainly to departmental expenditure in excess of supply issues, and to departmental payovers to the Consolidated Fund of monies received by departments (both in March and earlier). For the year as a whole, supply issues and actual departmental expenditure were almost exactly the same.

J.A. Clark

John Clark (ext 3093)
PSF Division, HM Treasury

CHANCELLOR OF THE EXCHEQUER

X [illegible]
[illegible]
last [illegible]
[illegible] smaller by
years ago
a emphasis of PRT
payments.
It was
at work
revising
this.

Ch.

Another front-end loading story – though only about 75% in the first half year compared with the 93% forecast this time last year (73½% in the event).

Perhaps the markets are beginning to understand – though it was still in HF3

I think I would be asking why we can't do a lot more to smooth the PSBR profile.

KC 17/4.

R3.47

FROM: MRS R LOMAX
DATE: 22 April 1985

MR CASSELL

cc Sir P Middleton
Sir T Burns
Mr H Evans
Mr Battishill
Mr Lankester
Mr Collinson
Miss Peirson
Mr Devereux
Dr Webb

MONTHLY NOTE ON THE PSBR

The Chancellor has seen Miss Peirson's note of 17 April and noted that we are once again expecting the PSBR to be unusually front-end loaded in the coming financial year. He thinks it would be worth reviewing the work that was done some years ago to see if there is anything further that we can do to smooth the PSBR profile.

RL

RACHEL LOMAX

R3.52 2 3 APR 1985

SECRET

cc CST Sir PM
FST
MST
EST
Sir P Middleton
Mr Anson
Mr Kemp
Miss Seammen
Mr D Williams
Miss Walker
Mr Cropper
Mr Lord

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

22 April 1985

The Rt Hon Norman Fowler MP
Secretary of State for Social Services
Department of Health and Social Security
Alexander Fleming House
Elephant & Castle
LONDON SE1

Dear Norman

SOCIAL SECURITY REVIEW - PUBLIC SERVICE PENSIONS

Your recent minute to the Prime Minister about your proposals for a new framework for occupational and personal pensions indicated that you would discuss separately with Treasury Ministers the implications of these proposals for the indexation of public sector pensions. While I am sure it would be wrong to include any specific reference to this in your Green Paper, the proposal that occupational and personal pension arrangements should, in respect of future benefit rights, have to provide as a minimum for the annual indexation of benefits in payment up to a maximum of 5 per cent, is likely to raise questions about our future policy on the existing indexation arrangements in public service and sector schemes.

Our present policy was set out in the 1983 Manifesto which said that "public sector pensioners will also be protected on the basis of realistic pension contributions". We discussed this in Cabinet on 15 September 1983, following which an Official Group was set up to look at this and other allied matters. We discussed their work in E(PSP) on 24 July last, and concluded, as I reported in my minute to the Prime Minister of 27 July, that the ways forward identified by officials were unattractive, and that the matter should be reviewed again following the outcome of your Inquiry into Provision for Retirement.

My view is that if the question of indexation of public service pensions is raised following publication of your Green Paper, we should take the line that your proposals have no necessary relevance. We would base this on the fact that our proposals for the future related to a minimum requirement for indexation, with nothing stopping those concerned doing better if they so wish; and that accrued rights under the present state earnings-related pension schemes (SERPS) will be honoured. If pressed, we should continue to rest on the Manifesto statement though indicating that the possibility of changes is not closed off, certainly on the contribution side. X

(+ PTO)

If you agree we could report it to Cabinet at the same time as we consider your Green Paper, on 25 April; and my officials could circulate for agreement with officials in interested Departments a form of words to be used when questions arise.

More generally I agree that if the framework you are to propose in your Green Paper is introduced, public service schemes must fit in with it. There are two particular points I should mention here. First, in most cases the schemes will have to be amended to allow employees to opt for personal pensions; and in the case of the Civil Service it will almost certainly be necessary, if the personal pension option is to be a reality, for us to find some way of moving to a contributory scheme. Second, although the cost may be substantial, we shall have to consider extending membership of the public service schemes down to include those part-timers earning above the lower earnings limit, if that is the condition which is in future to apply in the private sector.

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

Yours
Nigel

NIGEL LAWSON

Ch/ The skewness of CT wouldn't matter so much if it was offset by other things. So you don't have to confine this review to CT, as he implies.
RL
24/4

This was not what I had in mind. What I wanted was for us to look again at (a) PRT timing, (b) offsetting the CT skewness.
N

FROM: F CASSELL
24 April 1985

CHANCELLOR

cc Sir P Middleton
Sir T Burns
Mr Battishill
Mr Evans
Mr Lankester
Miss Peirson

PSBR PROFILE

You noted the front-end-loading expected once again in the PSBR this year, and suggested that it would be worth reviewing the work done some years ago, to see if there is anything further that we can do to smooth the PSBR profile.

On Cabinet folder

2. As Miss Peirson's note of 17 April said, the main reason why front-end-loading continues, and indeed has worsened lately, is the skewness of corporation tax receipts. In 1985-86, no less than 77 per cent of these receipts are expected to come in the second half of the year: if they were instead evenly distributed this would shift about £2¾ billion from the second to the first half of the year. Given the concentration of privatisation and PRT receipts in April/September the PSBR would then be strongly back-end-loaded, with about 35 per cent of it expected in the first half (instead of 75 per cent).

3. There are two reasons why corporation tax is having a more marked effect on the profile: the partial replacement of National Insurance Surcharge (an evenly-distributed tax) by additional corporation tax, and the continuing growth - very strong recently - in profits. The forecast increase of £2 billion in corporation tax in 1985-86 over 1984-85 has alone increased the front-end-loading of the PSBR by around 8 per cent, ie from the 67 per cent average in the 7 years up to and including 1984-85, to 75 per cent.

4. The increasing importance of CT has outweighed the effects of the other changes we have made, following the review 4½ years ago, to smooth the profile of the PSBR. I will explore again

with Inland Revenue the possibility of advancing the receipts of corporation tax during the year. There are difficulties - as we have found whenever we have looked at this in the past - but conditions may now be more favourable to introducing such changes than was the case 4 years ago. I will report back to you.

F CASSELL

SECRET

FROM: MISS G NOBLE

DATE: 29 April 1985

CHANCELLOR

cc PS/Chief Secretary
APS/Minister of State
Sir P Middleton
Mr Bailey OR
Sir T Burns
Mr Anson
Mr Kemp
Mr Watson
Mr Cropper
Mr Lord

SERPS: BRIEFING FOR PRIME MINISTER'S MEETING

Compulsory Scheme

You asked for a note on the fall back position of a rather better compulsory scheme.

2. The main point is the one Sir T Burns mentioned. Namely if the aim is to keep people off supplementary benefit why oblige them to do more. If 4 per cent of, say, £150 a week is enough to do the job, why require 4 per cent for someone earning £250 a week. It only takes a few pounds more than the basic pension to keep people off supplementary benefit. (Earnings dynamism of private provision only really required if we expected to uprate SB by earnings over the next 50 years).

3. There are a number of problems on mechanics including how we police the system, (especially the self employed) what do we do with defaulters, is the scheme to be based on cumulation of earnings, will we be able to get the providers to set up a clearing house (probably not, in which case there are IR or DHSS staff implications) etc. These sort of issues were raised at an official meeting with DHSS. The minutes attached are the best source of further points if you have time to read it.

pp. Stephanie K Holman

G NOBLE

21

FROM:- R J DEVEREUX

DATE:- 2 MAY 1985

1. MISS PEIRSON MP

2. CHANCELLOR OF THE EXCHEQUER

cc Sir P Middleton
Sir T Burns
Mr Cassell
Mr H P Evans
Mr Battishill
Mr Lankester
Mr Collinson
Dr I Webb

Thanks. NL.

CGBR IN APRIL

The preliminary estimate of the CGBR in April is £0.9 billion, and the estimate of borrowing by central government on its own account - CGBR(O) - is £1.1 billion. These figures are not yet firm and may change with later information before publication on 17 May in the monthly press notice on the PSBR.

2. The CGBR(O) outturn is £0.6 billion lower than the forecast made a month ago. The main factors are higher Customs and Excise receipts (by £0.2 billion), higher Inland Revenue receipts (by £0.1 billion), and apparently lower supply expenditure.

3. On-lending to local authorities was £0.3 billion lower than forecast.

4. Further analysis of the outturn in April will be given in the next Ministerial monthly note on the PSBR in two weeks' time.

R J DEVEREUX

CENTRAL GOVERNMENT TRANSACTIONS (2)

£ billion

	Inland Revenue	Customs & Excise	Other own account	CGBR(O)	Net Lending LAs	Net Lending PCs	CGBR
1st April 1985 - 30 April 1985							
Outturn (1)	+ 3.8	+ 3.3	- 8.2	- 1.1	-	+ 0.2	- 0.9
Budget profile	+ 3.7	+ 3.1	- 8.5	- 1.7	- 0.3	+ 0.1	- 1.9
Difference	+ 0.1	+ 0.2	+ 0.3	+ 0.6	+ 0.3	+ 0.1	+ 1.0
1st April 1984 - 30 April 1984	+ 3.3	+ 2.5	- 7.7	- 1.9	- 0.2	+ 0.2	- 1.9
Calendar April 1985							
Outturn (1))							
Last month's forecast) as above							
Difference)							

(1) Preliminary estimate, subject to revision

(2) + indicates a receipt, net receipt, or difference which reduces the CGBR

- indicates a payment, net payment, or difference which increases the CGBR

P2.56

CONFIDENTIAL

FROM: P WYNN OWEN
DATE: 7 May 1985

MR R J DEVEREUX

cc Sir P Middleton
Sir T Burns
Mr Cassell
Mr H P Evans
Mr Battishill
Mr Lankester
Miss Pierson
Mr Collinson
Dr I Webb

CGBR IN APRIL

The Chancellor has seen and was grateful for your minute of 2 May.

PWO.

P WYNN OWEN

GOVERNMENT ACTUARY'S DEPARTMENT
22 KINGSWAY LONDON WC2B 6LE
TELEPHONE 01-242 6828 Ext 312

7 May 1985 SECRET

Sir Peter Middleton
H M Treasury
Parliament Street
London SW1P 3AG

cc Mr Byatt
Mr Battishill

Dear Sir Peter

PHASED ABOLITION OF SERPS

Following our meeting with the Chancellor yesterday, I have devised what might be a feasible scheme for phasing the abolition of SERPS. The aim was to remove cliff edges in benefit expectations at particular ages, to reduce the increase in NICs by adopting a less deep taper for low wage-earners and to phase in the introduction of the compulsory occupational scheme in a way consistent with the phased abolition of SERPS and so as to lessen the immediate PSBR effects.

The resulting scheme is set out in detail in Annex 1. Its main features are:

* full SERPS entitlement for everyone retiring up to 5 April 1998

* accrued SERPS rights only (on GMP accrual formula with earnings dynamism) for those retiring from 6 April 2005 onwards

* some further SERPS build-up (on a sliding scale) for those retiring between 6 April 1998 and 5 April 2005

* compulsory scheme starts at 6 April 1987 at 2% level of contribution for everyone than aged under 53

* contributions under compulsory scheme rise at 6 April 1989 to 3% for everyone aged under 53 at that date

* contributions under compulsory scheme rise at 6 April 1991 to 4% for everyone aged under 53 at that date

* NICs phased in correspondingly with main rate of 16.0% and those still in SERPS paying a supplement

* contracted out rebate would be halved in 1987/88 to 3.15% with GMPs accruing a half rate for that year

* everyone below 49 at 6 April 1987 would accrue AC for 1987/8 at half the current rate

* no contracting out from 1988/89 except as basis for granting older employees in good pension schemes exemption from the supplementary NIC rate

* the NICs for the low paid would be 4%/6%/8% from 6 April 1988

The resulting changes in burdens are shown in Annex 2. We have attempted to work these through to the tables which we have become accustomed to seeing with each option, but this is just a rough first attempt. These show 1987/88, 1988/89, 1989/90 and an ultimate position on 1989/90 economic assumptions (i.e. if it had been reached then, whereas it will in fact be reached in 1991/92).

We have not yet been able to do a proper analysis of the long term benefit costs of this scheme. The savings would clearly be a little lower than under the scheme discussed yesterday but would probably still be of the order of £20 billion in 2033/34.

I am sending copies of this letter and attachments to Sir Terence Burns, Alan Bailey, Peter Kemp, Gerald Watson, Diana Seammen and Gill Noble.

Yours sincerely

Chris Daykin

C D Daykin

ANNEX 1

PHASED ABOLITION OF SERPS

SERPS ENTITLEMENT

Everyone reaching retirement age (65M/60F) up to 5 April 1998 would reach full expected benefits under SERPS.

Those reaching retirement age after 6 April 2005 would receive only their accrued SERPS rights earned up to 5 April 1988. These would be expressed in terms of the GMP accrual formula, with earnings revaluation up to retirement age. The year 1987/88 would count at half the existing accrual rate.

Those reaching retirement age between 6 April 1998 and 5 April 2005 would receive SERPS benefits based on the following percentages of revalued average earnings (RAE) above the LEL for full careers since SERPS began.

Retiring	Percentages of RAE
Between 6.4.98 and 5.4.99	25
Between 6.4.99 and 5.4.00	22½
Between 6.4.00 and 5.4.01	20
Between 6.4.01 and 5.4.02	17½
Between 6.4.02 and 5.4.03	15
Between 6.4.03 and 5.4.04	12½
Between 6.4.04 and 5.4.05	10

COMPULSORY SCHEME

Compulsory occupational pension provision at a level of a 2% contribution (1% employee, 1% employer) would be introduced from 6 April 1987 for everyone aged under 53 at that date.

The compulsory level of contribution would be increased to 3% (1½% employee, 1½% employer) from 6 April 1989 for everyone aged under 53 at that date.

The level of contribution required be finally increased to 4% (2% employee, 2% employer) from 6 April 1991 for everyone aged under 53 at that date.

Thus from 6 April 1991 onwards everyone who was under 49 on 6 April 1987 would have to contribute at 4%, those aged 49 to 51 on 6 April 1987 would have to contribute at 3% and those aged 51 to 53 on 6 April 1987 would have to contribute at 2%.

NICs

The standard joint rate of NIC would be as follows:

1987/88	1988/89	1989/90	Ultimate*
17.4	16.0	16.0	16.0

* on 1989/90 assumptions

These would be paid in respect of the contracted in aged 49 and under (at 6 April 1987) in 1987/88 and by everyone aged 49 and under (at 6 April 1987) in subsequent years. They would also be paid in respect of older employees in contracted out schemes (i.e. which are contracted out now and remain in force in much the same form). Employees over 49 at 6 April 1987 who remain in SERPS would pay a supplementary contribution (split 50:50 between employees and employers) as follows:

Age at 5 April 1987	Supplementary contribution	Period
49 to 51	1%	6 April 1991 onwards
51 to 53	1%	6 April 1989 to 5 April 1991
	2%	6 April 1991 onwards
53 and over	2%	6 April 1987 to 5 April 1989
	3%	6 April 1989 to 5 April 1991
	4%	6 April 1991 onwards

The contracted out rebate would fall to 3.15% (1.10% employee, 2.05% employer) for 1987/88 and would disappear altogether from 6 April 1988.

Standard rates of NIC for the lower paid would be 4½%/6½%/8½% (employees) and 4½%/6½%/8½%/8.9% (employers) in 1987/88, falling to 4%/6%/8% (employees) and 4%/6%/8% (employers) in 1988/89 and subsequently.

ANNEX 2

CHANGES IN NIC BURDENS

£ (million)	1987/88	1988/89	1989/90	Ultimate* (say)
Contracted in				
Employers	- 10	- 640	- 630	- 590
Employees	- 310	- 580	- 540	- 500
Contracted out				
Employers	+ 150	+ 730	+ 760	+ 760
Employees	+ 170	+ 510	+ 530	+ 530

* on 1989/90 assumptions

Standard rate of NIC	17.4	16.0	16.0	16.0

PHASED REPLACEMENT OF SERPS BY INTRODUCTION OF MINIMUM PRIVATE PENSION CONTRIBUTION; SERPS PRESERVED FOR OLDER WORKERS WITH PHASED RUN IN OF ACCRUAL

A. OVERALL IMPACT ON PUBLIC EXPENDITURE AND PSBR

(£ billion)	1987-1988	1988-1989	1989-1990	Ultimate**
Public Expenditure				
- savings agreed by MISC 111	- 0.3	- 0.5	- 0.5	- 0.5
- higher public sector employers' NIC	0	+ 0.3	+ 0.3	+ 0.3
- *higher public sector pension contributions	0	+ 0.1	+ 0.1	+ 0.1
Total public expenditure	- 0.3	- 0.1	- 0.1	- 0.1
Revenue				
- lower rate rebates	+ 0.5	+ 0.5	+ 0.5	+ 0.5
- tax relief on contributions	- 0.1	- 0.2	- 0.2	- 0.4
- NICs: private sector	NIL	- 0.3	- 0.2	- 0.1
public sector	0	+ 0.3	+ 0.3	+ 0.3
- higher public sector pension contributions	0	+ 0.1	+ 0.1	+ 0.1
Total Revenue	+ 0.4	+ 0.4	+ 0.5	+ 0.4
Total PSBR	- 0.7	- 0.5	- 0.6	- 0.5
of which:				
MISC 111	- 0.8	- 1.0	- 1.0	- 1.0
SERPS	+ 0.1	+ 0.5	+ 0.4	+ 0.5

* This assumes that public sector employees not now covered are brought into (new) schemes at the minimum required level.

** On 1989/90 assumptions.

B. 'BURDEN' ON ECONOMY

	1987/88	£ million
Private sector employers		400 loss
All employees		100 loss
Self-employed		No change
PSBR		100 loss
Total Burden		600 loss

	1988/89	£ million
Private sector employers		No change
All employees		100 loss
Self-employed		No change
PSBR		500 loss
Total Burden		600 loss

	1989/90	£ million
Private sector employers		100 loss
All employees		400 loss
Self-employed		No change
PSBR		400 loss
Total Burden		900 loss

	Ultimate*	£ million
Private sector employers		200 loss
All employees		500 loss
Self-employed		No change
PSBR		500 loss
Total Burden		1200 loss

* on 1989/90 assumptions

C. EFFECTS ON DIFFERENT SECTORS

(£ billion)	1987-1988	1988-1989	1989-1990	Ultimate**
<u>Effects on private sector employers' costs</u>				
- Extra NICs	+ 0.1	- 0.2	- 0.2	- 0.1
- Contributions to private schemes	+ 0.3	+ 0.3	+ 0.4	+ 0.5
- Gross increase in employers' costs	+ 0.4	+ 0.1	+ 0.2	+ 0.4
- less tax relief	0	- 0.1	- 0.1	- 0.2
Net increase in employers' costs	+ 0.4	NIL	+ 0.1	+ 0.2
<u>Effects on private and public sector employees</u>				
- Extra NICs	+ 0.1	- 0.1	-	-
- Contributions to private schemes	+ 0.3	+ 0.3	+ 0.5	+ 0.7
- Gross increase	+ 0.2	+ 0.2	+ 0.5	+ 0.7
- less tax relief	- 0.1	- 0.1	- 0.1	- 0.2
Net increase (i.e. employers' costs reduction in take-home pay)	+ 0.1	+ 0.1	+ 0.4	+ 0.5
<u>Effect on self-employed</u>		UNCHANGED		

*on 1989/90 assumptions

D. EFFECTS ON CONTRACTED-IN AND CONTRACTED OUT

(i) 1987/88

(£ billion)	Contracted-out	Contracted-in	Total
<u>Effects on private sector employers' costs</u>			
Extra NICs	+ 0.1	-	+ 0.1
Contributions to private schemes	-	+ 0.3	+ 0.3
Gross increase in employers' costs	+ 0.1	+ 0.3	+ 0.4
less tax relief	-	- 0.1	- 0.1
Net increase in employers' costs	+ 0.1	+ 0.2	+ 0.3
<u>Effects on private and public sector employees</u>			
Extra NICs	- 0.3	+ 0.2	- 0.1
Contributions to private schemes	-	+ 0.3	+ 0.3
Gross increase	- 0.3	+ 0.5	+ 0.2
less tax relief	-	- 0.1	- 0.1
Net increase (i.e. reduction in take-home pay)	- 0.3	+ 0.4	- 0.1

D. EFFECTS ON CONTRACTED-IN AND CONTRACTED OUT

(i) 1988/89

(£ billion)	Contracted-out	Contracted-in	Total
Effects on private sector employers' costs			
Extra NICs	+ 0.3	- 0.5	- 0.2
Contributions to private schemes	-	+ 0.3	+ 0.3
Gross increase in employers' costs	+ 0.3	- 0.2	+ 0.1
less tax relief	-	- 0.1	- 0.1
Net increase in employers' costs	+ 0.3	- 0.3	NIL
Effects on private and public sector employees			
Extra NICs	- 0.6	+ 0.5	- 0.1
Contributions to private schemes	-	+ 0.3	+ 0.3
Gross increase	- 0.6	+ 0.8	+ 0.2
less tax relief	-	- 0.1	- 0.1
Net increase (i.e. reduction in take-home pay)	- 0.6	+ 0.7	+ 0.1

D. EFFECTS ON CONTRACTED-IN AND CONTRACTED OUT

(i) 1989/90

(£ billion)	Contracted-out	Contracted-in	Total
<u>Effects on private sector employers' costs</u>			
Extra NICs	+ 0.4	- 0.6	- 0.2
Contributions to private schemes	-	+ 0.4	+ 0.4
Gross increase in employers' costs	+ 0.4	- 0.2	+ 0.2
less tax relief	-	- 0.1	- 0.1
Net increase in employers' costs	+ 0.4	- 0.3	+ 0.1
<u>Effects on private and public sector employees</u>			
Extra NICs	- 0.5	+ 0.5	-
Contributions to private schemes	-	+ 0.5	+ 0.5
Gross increase	- 0.5	+ 1.0	+ 0.5
less tax relief	-	- 0.1	- 0.1
Net increase (i.e. reduction in take-home pay)	- 0.5	+ 0.9	+ 0.4

D. EFFECTS ON CONTRACTED-IN AND CONTRACTED OUT

(i) Ultimate

(£ billion)	Contracted-out	Contracted-in	Total
<u>Effects on private sector employers' costs</u>			
Extra NICs	+ 0.4	- 0.5	- 0.1
Contributions to private schemes	-	+ 0.5	+ 0.5
Gross increase in employers' costs	+ 0.4	-	+ 0.4
less tax relief	-	- 0.2	- 0.2
Net increase in employers' costs	+ 0.4	- 0.2	+ 0.2
<u>Effects on private and public sector employees</u>			
Extra NICs	+ 0.5	- 0.5	-
Contributions to private schemes	-	+ 0.7	+ 0.7
Gross increase	+ 0.5	+ 0.2	+ 0.7
less tax relief	-	- 0.2	- 0.2
Net increase (i.e. reduction in take-home pay)	+ 0.5	NIL	+ 0.5

SECRET

ECONOMIC IMPLICATIONS OF INCREASING PENSION FUND INCOME

Note by the Chief Economic Adviser

The phased abolition of SERPS and the introduction of compulsory private pension arrangements have three components from an analytical point of view. It is helpful to separate them although in practice they are interdependent:

i. the implied lower scale of compulsory pension provision;

ii. the switch from PAYG to a fully funded scheme;

iii. the privatisation of the scheme.

Reduction in Compulsory Pension Provision

2. The proposed scheme involves a lower scale of compulsory pension provision. The proposed minimum compulsory contribution rate of 4 per cent to private schemes is less than the 8 per cent contribution rate for a new entrant that is estimated to be required if SERPS is to be fully funded. Hence there will be some reductions in future pension income if private contributions are at the minimum level.

3. The argument for reducing the scale of compulsory pension provision under the present unfunded SERPS arrangements is that there are expected to be very high NI contribution rates when SERPS matures. These will have adverse supply side effects because of their impact on incentives and enterprise. If SERPS were replaced by funded schemes there would have to be an increase in contribution rates immediately.

Switch from PAYG to a fully-funded Scheme.

4. The most important macro-economic aspect of the proposal is the change from PAYG to full funding. Such a shift would be important whether the fund is in the

private or public sector. The switch to full funding requires an increase in contributions in the period until SERPS would have matured. A fully funded public sector scheme would mean a lower PSBR; a fully-funded private sector scheme means increased contributions to private pension funds. In either case contributions by companies will increase and the take-home pay of employees will be reduced. This is the inevitable consequence of funding.

5. The effect of the move from PAYG to full-funding is to increase the amount of saving and investment which the economy as a whole undertakes, at the expense of consumption. The result will be a build-up of assets which will provide later generations with the income from which to finance pensions, so easing the burden on future workers. The additional investment is likely to be both domestic and overseas. Interest rates and the exchange rate are likely to be lower and the balance of payments on current account will be improved, and this will be matched by investment abroad.

6. The macro-economic effects of the switch to funding in the private sector are very similar to those of a switch to funding in the public sector. It makes little difference whether contributions are paid by employers and employees to the National Insurance Fund, and the Government uses the surplus on the Fund to reduce gilts sales; or they are paid to private pension funds which invest them in domestic and overseas financial markets. Either way the general level of interest rates and the exchange rate will be reduced although the structure of yields will differ.

7. The switch from PAYG to funding is likely to involve a transitional period of a few years during which output may be adversely affected. Essentially this arises because there tends to be a lag between the initial reduction in consumption that follows an increase in contributions and the subsequent rise in investment and net exports induced by the lower interest rates and exchange rate. But employment costs would be higher and take-home pay lower. This reduction in output is unlikely to be as much as a ½ per cent at its peak.

8. The transitional impact on output from a move to a private sector funded scheme could be offset by an equivalent increase in the PSBR. This would have the effect of offsetting the higher private sector savings by higher public sector borrowing and effectively undo the switch to funding. Taxes could be reduced on both employers and employees, thus "matching" the increased pension contributions. But, of course, there would be presentational difficulties in explaining a higher PSBR simply because of higher flows to pension funds.

9. Another possibility is that the private sector reduces its other savings and increases its borrowing to offset the effect of higher savings in the pension funds. This is most likely in the case of personal pensions but the scale of this is unlikely to be large, particularly in the short-term.

Privatisation of Pensions

10. In addition to the macro-economic effects of switching to fully funded pensions in the private sector, there are other relevant aspects of privatisation.

11. Financial Markets. The efficiency of financial markets may be affected by the greater proportion of all financial intermediation that is undertaken by pension funds after privatisation. The direction and extent of the effect depends on the efficiency of pension funds compared with other financial intermediaries. We have little evidence on which to base a judgement about this.

12. Individual Choice. Schemes in the private sector could - in certain circumstances - be more responsive to individual needs than public sector schemes. The development of personal pension schemes could increase choice and enable contributors to build up individual property rights. This would, of course, be at the expense of some increase in the risk borne by individuals; the risk spreading inherent in the state scheme and present in many occupational schemes would be impossible. These risks would be large if financial markets were volatile. In present conditions, however, most private pension provision is in the form of occupational schemes, where employees have only limited choice about contribution rates, benefit levels, or the investment of funds.

13. Mobility of Labour. If privatisation were to take the form of more occupational pension schemes, which are less portable than SERPS, labour mobility would be reduced. Cross-subsidisation is inherent in occupational pension schemes. This reduces the risk borne by individuals but inevitably it limits the extent to which they can be transferred from one job to another. Early leavers suffer relative to those who remain with a single employer.

14. Administrative Burden. The administrative burden of operating a compulsory private scheme could be severe, particularly for those employers with a significant number of employees on low earnings. Operating private schemes will be more complicated than SERPS.

14. Administrative Burden. The administrative burden of operating a compulsory private scheme could be severe for small businesses not contracted out. Operating private schemes will be more complicated than SERPS.

Summary

15. The main points can be summarised as follows:

a. the argument for a reduction in the scale of compulsory pension provision is that, under the existing arrangements, there will be a major rise in contributions with consequential adverse supply side effects, and, under a funded scheme, there would have to be a significant increase in contributions when the funds were set up;

b. a switch from PAYG to a fully-funded scheme is likely to increase saving and investment and hence provide later generations with more income from which to finance pensions;

c. there will be a transitional period of a few years during which output will be marginally lower than otherwise; this could be offset in part by higher public sector borrowing but this could be presentationally difficult and would undo the move to funding future obligations;

d. the bulk of the effects stemming from privatisation are likely to be micro in nature. There may be some improvement in the efficiency of financial markets but we have no basis for believing it is likely to be large. They give more consumer choice but at the cost of increased individual risk. Labour mobility is likely to be damaged as private schemes do not deal as well as SERPS with those who change jobs. And the administrative costs of operating compulsory private pensions could be significant for small businesses not contracted out.

H.M. TREASURY
3rd May, 1985.

'Burden Tables

(i) Key point is that total burden is unalterable; distribution can be altered by policy changes.

(ii) Now assumed that self-employed neither contribute to compulsory scheme nor pay any extra NICs.

(iii) As compared with previous figures, much less redistribution between contracted in and contracted out at end of phasing ie 1989/90.

(iv) For contribution rates, see attached table.

Compulsory scheme - main features

(i) Contribution rate taken as 4%.

(ii) No UEL assumed for sake of simplicity.

(iii) Very rough figures suggest in ultimate, perhaps 300,000 dependent on supplementary benefit (likely to be underestimate), as compared with 100,000 on full SERPS.

Contracted-in
Contracted out 3¼
ave 2½%

(iv) For administration, coverage, see attached note.

(v) Women are assumed to draw full compulsory pension at 65; but can take abated pension (60% of full) at age 60.

'Over 50's' scheme

3% = 3.7bn

(i) Assumed that all those retiring before April 2000 would retain full SERPS rights (ie men now over 50, women now over 45).

2/3 = 1/2p

(ii) Full effect on individuals, see attached tables.

(iii) They show 'cliff' produced by scheme; eg man on £200 per week would get £33.0 per week pension if just out of scheme, £52.50 per week if just in scheme.

(iv) This difference is not reflected in contribution rates; both pay the same ie 20.45%; only difference is that man outside scheme attracts tax relief on his share of 4% compulsory contribution.

(v) Suggests, in practice, scheme unacceptable; similar results will be produced by any scheme which operates sharp cut-off.

(vi) Suggests need for fuller taper, for those retiring beyond year 2000; complications becoming unbearable.

(vii) Or 10 year phasing out of SERPS for everyone; more equitable but would not wholly protect over 50s, if this is objective.

Public expenditure cost of SERPS

(i) See table; extra cost of phasing plus over 50s in line 5 is small.

(ii) But would be increased if further protection were given to those approaching 50.

'MISC 111 Bottom Line'

See overall impact table

PSBR effect

	1987/8	1988/9	1989/90
Non-SERPS	-0.8	-1.0	-1.0
SERPS	+0.1	+0.3	+0.6
	-0.7	-0.7	-0.4

Public expenditure effect

	1987/8	1988/9	1989/90
	-0.2	-0.2	-0.1

Other points

(i) End of SERPS could mean worse labour mobility (SERPS is fully transferable, no matter whether individual is contracted in or out, no matter how many jobs).

(ii) End of SERPS means end of earnings related component of invalidity benefit ie hitting long term sick, and

(iii) end of earnings related widows pensions; survivors benefits in new compulsory scheme will not compensate.

SECRET

NATIONAL INSURANCE CONTRIBUTION RATES 1989/90

MINIMUM PENSION CONTRIBUTION FOR EMPLOYEES UNDER 47 (WOMEN) OR 52 (MEN) IN 1987

SERPS CONTINUES FOR EMPLOYEES ABOVE THESE AGES

CONTRACTED-OUT EMPLOYEES AND THOSE NOT IN SERPS PAY SAME NIC RATES

Joint Class 1 NI Contribution

For contracted-out older employees and all others not in SERPS	16.45%
For contracted-in older employees	20.45%

For all low earners, regardless of age and contracted-out/in status:
stepped rates of, successively, 6%, 10%, 14%

These rates take account of there being no increase in NIC rates for self-employed people

The rates are applied to all liable earnings (i.e. there is no "contracted-out" band)

This will be the first year of the full minimum pension contribution: two years' phasing in is assumed, with minimum contributions of 2% and 3% in 1987/8 and 1988/9 respectively

SECRET

ANNEX 2

REPLACEMENT OF SERPS BY 3-YEAR PHASED INTRODUCTION OF MINIMUM PRIVATE PENSION CONTRIBUTION; SERPS PRESERVED FOR OLDER WORKERS

A. OVERALL IMPACT ON PUBLIC EXPENDITURE AND PSBR

(£ billion)	1987/88	1988/89	1989/90
Public Expenditure			
- savings agreed by MISC 111	- 0.3	- 0.5	- 0.5
- higher public sector employers' NICs	+ 0.1	+ 0.2	+ 0.3
- *higher public sector pension contributions	0	+ 0.1	+ 0.1
Total public expenditure	- 0.2	- 0.2	- 0.1
Revenue			
- lower rate rebates	+ 0.5	+ 0.5	+ 0.5
- tax relief on contributions	- 0.1	- 0.2	- 0.3
- NICs: private sector	0	- 0.1	- 0.3
public sector	+ 0.1	+ 0.2	+ 0.3
- higher public sector pension contributions	0	+ 0.1	+ 0.1
Total Revenue	+ 0.5	+ 0.5	+ 0.3
Total PSBR	- 0.7	- 0.7	- 0.4
of which:			
MISC 111	- 0.8	- 1.0	- 1.0
SERPS	+ 0.1	+ 0.3	+ 0.6

* This assumes that public sector employees not now covered are brought into (new) schemes at the minimum required level.

B. 'BURDEN' ON ECONOMY

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

	1987/88 £ million
Private sector employers	300 loss
All employees	200 loss
Self-employed	No change
PSBR	100 loss
Total Burden	600 loss

	1988/89 £ million
Private sector employers	300 loss
All employees	400 loss
Self-employed	No change
PSBR	300 loss
Total Burden	1,000 loss

	1989/90 £ million
Private sector employers	200 loss
All employees	500 loss
Self-employed	No change
PSBR	600 loss
Total Burden	1,300 loss

C. EFFECTS ON DIFFERENT SECTORS

(£ billion)	1987/88	1988/89	1989/90
Effects on private sector employers' costs			
Extra NICs	0	- 0.1	- 0.3
Contributions to private schemes	+ 0.3	+ 0.5	+ 0.6
Gross increase in employers' costs	+ 0.3	+ 0.4	+ 0.3
Less tax relief	0	- 0.1	- 0.1
Net increase in employers' costs	+ 0.3	+ 0.3	+ 0.2
Effects on private and public employees			
Extra NICs	0	0	0
Contributions to private schemes	+ 0.3	+ 0.5	+ 0.7
Gross increase	+ 0.3	+ 0.5	+ 0.7
Less tax relief	- 0.1	- 0.1	- 0.2
Net increase (ie reduction in take-home pay)	+ 0.2	+ 0.4	+ 0.5
Effect on self-employed			
Extra NICs			
Less tax relief		U N C H A N G E D	
Net increase			

D. EFFECTS ON CONTRACTED-IN AND CONTRACTED-OUT

(i) - 1987/88

(£ billion)	Contracted-out	Contracted-in	Total
Effects on private sector employers' costs			
Extra NICs	+ 0.2	- 0.2	0.0
Contributions to private schemes	0.0	+ 0.3	+ 0.3
Gross increase in employers' costs	+ 0.2	+ 0.1	+ 0.3
Less tax relief	0.0	0.0	0.0
Net increase in employers' costs	+ 0.2	+ 0.1	+ 0.3
Effects on private and public employees			
Extra NICs	+ 0.2	- 0.2	0.0
Contributions to private schemes	0.0	+ 0.3	+ 0.3
Gross increase	+ 0.2	+ 0.1	+ 0.3
Less tax relief	0.0	- 0.1	- 0.1
Net increase (ie reduction in take-home pay)	+ 0.2	0.0	+ 0.2

ANNEX 3

ISSUES RAISED AT MEETING ON 1 MAY 1985

Contributions to National Insurance scheme and Compulsory Scheme

1. The assumptions about the structure of contributions are set out in the description of the proposal in Annex 1.

2. The minimum level of contribution to the compulsory scheme has been taken as 4%. The figures in Annex 2 reflect this. But, of the 4%, ½% is required to cover the cost of survivorship (widows') benefits for those under pension age. Only 3½% goes towards the pension payable at retirement.

3. A contribution level of 5% would produce higher pensions and reduce the proportionate cost of administration. But it would add to employers' and employees' costs. A contribution level of 3% would have opposite effects: less cost but lower pensions. However, a 3% contribution would leave substantially more people requiring means-tested help.

4. The effects of different contribution levels on the numbers requiring help under the new income support scheme which will replace supplementary benefit are estimated below:

NUMBERS RECEIVING SUPPLEMENTARY PENSION

OPTION	SUPPLEMENTARY PENSIONERS IN:		
	1985-86	1994-95	2035-36
1. Full SERPS continued.	1,630,000	970,000	100,000
2. SERPS replaced compulsory contributions of:			
(a) 5%	1,630,000	1,050,000	250,000
(b) 4%	1,630,000	1,115,000	300,000
(c) 3%	1,630,000	1,250,000	500,000

Note: assumes prices upratings of benefits.

5. The framework in Annex 1 assumes that the upper earnings limit for National Insurance cotributions applies, as announced in the Budget, to employees but not employers. The framework also assumes no limit for the new compulsory contributions. This is certainly simpler. But it also takes account of the fact that the great majority of higher earners will already be covered by qualifying pension arrangements so that in practice they will not be affected. On the other hand, introducing a limit(eg at 1½ times average earnings as for National Insurance contributions) might make the proposal more acceptable to those employers who have criticised the abolition of the UEL for employers' contributions in the Budget.

SECRET

ADMINISTRATION OF THE COMPULSORY SCHEME

1. Administration of the compulsory scheme will be kept as simple as possible. The aim will be to use and build on machinery which already exists in the DHSS and Inland Revenue for tax approval of schemes, supervision of those which are contracted-out from SERPS, and the collection and checking of national insurance contributions (NIC). The system will build on the DTI White Paper proposals for investor protection. Officials of DHSS and DTI are exploring how this would work in practice.

Requirements of the scheme

2. All occupational pension schemes have to be scrutinised and approved by the Inland Revenue Superannuation Funds Office before investments and income can be tax-exempt and contributions to them qualify for relief. This scrutiny will be the principal means of ensuring that participating schemes are bona fide.

3. Schemes which are contracted-out from SERPS will satisfy the conditions of the compulsory scheme automatically. Appropriate parts of the present supervisory machinery operated by the Occupational Pensions Board and DHSS' Newcastle Central Office can be kept in place to ensure that they continue to do so. This machinery could also provide a back-up check on new schemes if necessary.

4. Pay-as-you-go public service schemes will be safeguarded and not subjected to onerous checks. All that they will be required to provide are undertakings that scheme benefits correspond with those to be obtained from the compulsory scheme.

5. An essential feature of the scheme is that employees will be able to opt for a personal pension instead of joining an employer's scheme. And employers will be able to meet their obligations by offering employees personal pensions. The minimum total contribution and the employer's share will be the same as for occupational schemes. For employees personal pensions will mean more choice and flexibility. For employers - especially small ones - they will offer a way of satisfying the requirements of the new arrangements without having to set up a scheme of their own.

SECRET

6. Industry-wide schemes would be another means of keeping down burdens on employers, particularly small ones. They would cater for frequent job-changers, who are disproportionately represented in industries with low coverage now, e.g. catering and construction.

7. Employers who wish to set up schemes will be able to do so either by establishing their own self-administered trusts or by making arrangements with life offices, friendly societies or other approved providers. The Green Paper will canvass a proposal that a wide range of financial institutions, besides insurers, should be permitted to offer pensions savings schemes. The list might include banks, building societies and unit trusts. Unless such bodies set up insurance company subsidiaries, insurance law will require them to sub-contract risk business (i.e. mainly survivors' benefits and the provision of annuities at retirement). Trustees of self-administered schemes and commercial providers will be required to supply employers with statements from appropriate professionals (e.g. lawyers and actuaries) that all statutory requirements are met. These statements will have to be kept by employers for inspection on demand by DHSS inspectors.

Operation

8. Employers will be required to deduct pension contributions from pay and pass them with their own contributions over to schemes. This requirement will extend to personal pensions taken as alternatives to membership of employers' own schemes. The contributions will be recorded on tax deduction documents, which are subject to end-of-year computer reconciliation at DHSS' Newcastle Central Office. The documents will be supported by confirmation from scheme trustees or commercial providers that contributions have been received. Again, this confirmation will be kept available for inspection on demand by DHSS. Computer reconciliation will show if pension contributions have not been paid for particular employees or have been paid at insufficient levels. Queries will be dealt with in just the same way as when these checks show non- or inaccurate payment of NIC - by telephone and written enquiries, and visits by DHSS contribution inspectors. The manpower cost for DHSS has been provisionally estimated to be in the region of 250+ staff.

Flexibility and transfers

9. Because the new arrangements are based on money purchase principles, they will give people a new flexibility. Employees will be able to decide, according to their circumstances, whether take-home pay or savings are more important to them. Those with heavy commitments - e.g. younger workers with families - may choose to put only the minimum contribution into their occupational or personal pension. As they grow older and their commitments decrease, they may prefer to set aside more of their earnings towards their retirement (following the pattern already set by the self-employed). The new framework will give people the freedom and responsibility to set their own priorities.

10. An essential part of this flexibility is that pension rights should be readily transferable. Neither employers nor employees will welcome a system that leaves people at retirement with small amounts of pension from many different sources.

11. In practice, transferability should not be a problem. An advantage of money purchase arrangements is that they give individuals an identifiable sum of pension savings that they can take with them when they change jobs or switch into a different type of investment. Appropriate controls will ensure that unfair administrative charges do not eat into those savings when they are transferred. And employers could be enabled to transfer into a personal pension the accrued rights of a leaving employee with less than, say, five years' service who does not opt for this himself. The current Social Security Bill will take care of schemes that offer salary-related benefits, by giving leaving employees the right to transfer the actuarial value of their pension rights.

FRAMEWORK OF THE COMPULSORY OCCUPATIONAL PENSION SCHEME

COVERAGE

Employees - including married women optants (reduced rate NI - no pension rights on own contributions) ?

Self-employed people: Green Paper to float covering them as logical; but prepared to back-track

? Not the non-employed (problem of policing, who would pay "employer's" contribution, and earmarking a percentage of benefit for "employee's" share)

how many? £bs, cost?

what proportion of women are covered — in that category?

EXCEPTIONS

People earning less than a certain amount. Simplest if the amount were equal to the LEL, but its double cliff-edge effect (NI contributions + 2% or 2½% for private cover) could exacerbate the poverty trap and worsen incentives

Very new employees (because of possible need to except casuals - 6 months or a year before inclusion compulsory)

Self-employed people with profits below a given level (probably tied to small earnings exception for Class 2 NIC)

People within 5 years of State pension age at start of scheme (very high contributions would be needed to get any appreciable pension return for them)

QUALIFYING SCHEMES

Defined contribution (group money purchase the norm)

Defined benefit schemes also able to qualify

Personal pensions

Retirement annuities ("section 226" schemes) for self-employed

QUALIFYING CONTRIBUTION

Joint employer/employee contribution of 5% or 4% ? earnings. Employer to contribute at least half but can qualify by contributing that percentage of his payroll to employees' pensions as a whole. But NB: need for some anti-discrimination provision to protect individuals if employer qualifies in this way.

Defined benefit schemes to qualify (those that had been contracted-out to do so automatically), possibly on basis of employer's average contribution over years, certified by scheme actuary.

Personal pension contributions at same level as group money purchase (4% or 5%), with employer obliged to meet at least half: but NB may buy less by way of pension, because administration costs more for individual than for group

Retirement annuity for self-employed with contribution at same level as joint rate for employer and employee.

QUALIFYING BENEFITS

Defined contribution schemes to provide sum to buy annuity on retirement. Everyone to have a free choice of where to buy their annuity, but must be uprated in line with lesser of 5% or RPI.

(Defined benefit schemes qualify on contribution test, but can provide pension related to salary, as now)

Survivors' benefits: as minimum, cover for surviving spouse aged 55 or over with dependent children. Lump sum insurance to secure pension possibly best way. Death in service and after retirement to be covered, including where marriage was after retirement.

No option of commuting part of pension savings into a lump sum.

EQUAL TREATMENT (very provisional)

? Equal contributions for both sexes. This will provide equal lump sum at a common age, possibly 65 (but with provision for lower pension at 60; or requirement to pay by 65 to accommodate schemes with lower retirement age).

? Unisex annuity tables to provide equal pensions from equal lump sums, a possibility if survivors' benefits cover widowers and marriages after retirement.

LEGISLATION

Could be prepared in 1985/6 for start of full compulsory scheme in 1987. But NB: need to ensure that any essential tax measures are in the 1986 Finance Bill.

Legislation to cover inclusions and exemptions; recognition of approved schemes; main survivors' benefits; right of employees to opt out of schemes for personal pensions. Powers to define bodies allowed to offer pension schemes; to define permitted investments (reserve power, for use only if needed); to set minimum contributions and to set level of earnings/gains at which employees/self-employed people must be covered.

PHASING (if needed)

? If not possible or desirable to introduce scheme in full in 1987 (eg because of reduced take-home pay and increased employment costs in an election year), phasing in could be on basis of inducement (preferential NI contribution rates) or compulsion in stages.

If by inducement, possibly phased and reducing NI concessions. Eg 3%, 2%, 1% in successive years, to encourage employers without schemes to come in early

If by phased compulsion (less favoured option), could be by size of workforce; by age of employee; by levels of earnings; by size of eligible payroll; or possibly size of turnover. Age or earnings of employee most clear-cut; but possibly simpler for employers to set up whole scheme at once.

RESIDUALS AND TRANSITIONALS

Possible need for blocking mechanism to prevent contracted-out schemes from transferring employees wholly or partly back into SERPS before its abolition, or buying back those with less than 5 years' service after SERPS goes.

GMPs to be preserved, and past pension rights to be preserved on same basis as before SERPS went (eg eightieths of final salary where this was the basis of scheme approval for contracting-out). If not, schemes get further profit from having been contracted-out.

Early leaver protection and transfer value rights still to apply.

ADMINISTRATION

Inland Revenue to give tax approval as now. DHSS to approve schemes as meeting compulsory requirements. Maximum coordination needed to cut out duplication and bureaucracy.

Self-regulatory bodies covering each type of provider to be responsible for general supervision including eg definition of permitted investments. (Reserve powers in legislation to be used only if needed: vested interest of bodies in getting large volume of new business gives strong incentive to ensure reputability).

Possibility of central schemes operated by providers to relieve eg small employers and self-employed of administration (NB: industry-wide schemes can help here too).

Control on administration charges needed. Otherwise "front-end loading" undermines buying value of contributions for low-paid workers changing jobs frequently. Industry-wide schemes could help again here and could sweep up frequent movers who may be disproportionately represented in industries with low scheme coverage - eg agriculture, construction, catering.

Central clearing house - to be set up by providers - neded for personal pensions, to save employer from having to deal with many different providers. Cannot restrict number of providers available to an employee with a particular employer, as this would remove choice and portability, which are the star attractions of personal pensions.

Employers responsible for deducting and paying over their own and employees' contributions. For personal pensions, employers to pay over to clearing house, as below.

OPERATION AND POLICING

Employers with group schemes submit to Inland Revenue of DHSS certification showing level of contributions to scheme with P35 (end of year schedule of pay and deductions) covering eligible employees.

For employees with personal pensions, employer sends contributions and single schedule (showing which provider each employee is with) to clearing house: it passes on contributions to provider. Providers notify Inland Revenue or DHSS at end of year of contributions paid for each personal pension holder. Contributions are checked against his record of earnings, to confirm enough has been paid.

Self-employed send certification of contribution paid to retirement annuity with audited accounts submitted for assessment to Inland Revenue. Checked to confirm represents minimum percentage of gains as accepted by the Revenue. This means (possibly many) self-employed with no or negative gains not contributing: unavoidable, if consistency with Revenue to be maintained.

Problem of how frequently employer should pay over contributions. Yearly is simplest - but difficulties of cash flow, insolvency during the year and cover for employees who have left. Needs further thought.

NON-COMPLIANCE, FRAUD AND INSOLVENCY

Financial penalties - possibly in form of "compounding", to cover payments due plus fine - for non-compliance. Further thought needed on using payments to cover employees where employer has not set up scheme.

Possible need for fund operated by institutions to underwrite losses from fraud and insolvency.

PUBLIC SECTOR

25% of public sector employees not now covered by schemes. Need to include them increases pubic expenditure, now for funded schemes, at retirement for others. But if covered at minimum required level, extra costs kept down because NI contribution rates for contracted-in drop after SERPS goes.

SCHEME FINANCES

A final problem. If minimum contribution to a personal pension is the same as for occupational schemes generally, it could create incentive for young employee to opt for personal pension. Possibly adverse effect if employers no longer have flexibility (within anti-discrimination safeguards) to tilt their minimum percentage of payroll contribution in favour of older employees.

- 8 MAY 1985

Sir PM

CONFIDENTIAL

FROM: E P KEMP
8 May 1985

MR D M WILLIAMS

cc ~~Sir~~ Peter Middleton
Mr Bailey
Mr Anson
Mr Watson
Miss Seammen
Mr Pain
Miss Walker

cc Sir T Burns
Mr Byatt
Mr Battishill

Is this complex worth a proposal to limit ... ?

PUBLIC SERVICE PENSIONS

I set out below an extract from a record of a meeting which the Prime Minister recently held, at which the Chancellor of the Exchequer and the Minister of State were present :-

> "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".

2. We have, of course, already put a paper to DHSS (seen by the Minister of State) on this question of personal pensions and possible costs of the PSBR. The assumption we took was that public sector employees would indeed be allowed to take personal pensions, whether or not they were in unfunded schemes, but that where this scheme was also non-contributory it was in effect a pretty unattractive option because it was difficult to see how we could assess the "employee" contribution some or all of which would have to be remitted to the provider of the personal pension in the case of people who took that option. The only clean solution we saw to this was to make such schemes - notably the PCSPS - overtly contributory. It would appear from the extract from the note I quote above, however, that the Chancellor has moved backwards on this, and seems to be querying whether or not personal pensions should be permitted

in such cases (as opposed to merely being pretty unattractive).

3. I should be grateful if you would give consideration to where we go from here. Purely from the point of view of preserving the PSBR at any rate in the short-term, we would like to prevent people in unfunded schemes taking personal pensions. But this may be hard to sustain; it would be seen as discrimination against public service employees and it would probably be unattractive to Mr Fowler and those others who see personal pensions as a desirable thing, and who ought not to want anyone to be estopped. We need to look out again the calculations that were made earlier as to the possible costs, and Ministers will have to be given a note as to the pros and cons of risking this cost. The second leg of the exercise will come if they agree that public sector employees should be allowed to take personal pensions, in the sense that if they do agree this they ought to be prepared to make it a reality, which means going for a contributory scheme.

E P KEMP

SIR P MIDDLETON

c Mr Anson
Mr Cassell
Mr Battishill
Mr Monger
Mr G P Smith

THE "NEW" STRUCTURE OF THE TAX SYSTEM

You enquired yesterday morning about progress on my work in setting out the post-Budget, post-Fowler structure of the tax system and the interactions with the Green Paper on transferable allowances. I think you had hoped to have a PCC discussion on 21 May.

2. Not unexpectedly, Mr Smee rang me yesterday afternoon, saying that their work - on which we depend critically - has been delayed by the recent discussions on SERPS, etc. These discussions have also heightened sensitivities about numbers and DHSS economists are under clear instructions to give their Green Paper top priority.

3. I have had to concede a week's delay on the work and so will not be able to write a PCC paper for discussion on 21 May. But unless we get further slippage, I should be able to make the following week.

4. The timetable is very tight - as it always has been. But DHSS assure me that provided there are no problems with Thursday's Cabinet and no further complications arise, they should be able to complete the work with a week's delay. I will do my best to make sure they deliver but we are very heavily dependent on their good offices. I will let you know if there is any further slippage.

IB

I C R BYATT

8 May 1985

FROM: MRS R LOMAX
DATE: 8 May 1985

cc Sir P Middleton
Sir T Burns
Mr Battishill
Mr Evans
Mr Lankester
Miss Peirson

MR CASSELL

PSP

PSBR PROFILE

The Chancellor has seen your minute of 24 April. He has commented that he was not particularly concerned about measures to smooth the CT profile; rather he thought that we ought to look again at the PRT timing, to see if there is anything that can be done to offset the skewness of corporation tax.

RL

RACHEL LOMAX

45

BF 22/5

CONFIDENTIAL

From: D R H BOARD

Date: 10 May 1985

MR BYATT

cc Mr Bailey
Sir T Burns
Mr Anson
Mr Cassell
Mr Kemp
Mr Battishill
Mr Monger
Mr Odling-Smee
Mr Watson
Mr Riley
Ms Seammen
Mr G P Smith
Mr D M Williams
Miss Noble

FOLLOWING THROUGH "FOWLER", ETC

Sir Peter Middleton was grateful for your minute of 8 May (entitled 'the "new" structure of the tax system') - copy attached for those who have not already seen it. Sir Peter agrees that the additional week's delay is disappointing. But it is understandable; all concerned are under considerable pressure. However Sir Peter would like to be quickly alerted if the delay looked like stretching further towards, say, 3 weeks.

2. As you know Sir Peter considers it important not to let up now on any of the aspects of work on the Fowler package; and he personally would like to be kept in touch with developments. It might be useful to jot a number of those aspects (so far as I am aware of them) down here:

(a) further macro-economic analysis;

- to take existing work deeper, and improve quantification,

- to embrace the non-SERPS elements of the Fowler package,

(**Action:** Sir T Burns)

(b) examination of GAD's proposal for phasing out SERPS (Daykin's letter of 7 May); further examination of detailed arrangements to be stipulated for phasing in compulsory, private provision; consideration of Green Paper re-drafts (ST to lead).

3. Sir Peter intends to hold a further meeting on social security in the next few weeks. Could ST keep me sufficiently in touch with developments so as to identify a suitable date/time?

X

Douglas Board

D R H BOARD
Private Secretary

CONFIDENTIAL AND PERSONAL

psr

FROM: MISS M E PEIRSON
DATE: 10 May 1985

1. MR CASSELL
2. CHANCELLOR OF THE EXCHEQUER

cc Sir P Middleton
Sir T Burns
Mr H P Evans
Mr Battishill
Mr Lankester
Mr Devereux
Dr I Webb
Mr Wells - CSO

PSBR IN APRIL

1. The first provisional outturn for the PSBR in February is £1.6 bn, £0.5 bn below the Budget profile (see table attached). Market expectations are between £1½ bn and £2¼ bn. Our estimate is subject to revision before publication on Friday 17 May.

2. The CGBR(O) in April was provisionally £1.1 bn, £0.6 bn below the Budget profile, as reported in Mr Devereux's note of 2 May. The main reasons for the difference from profile are, as he said, higher Customs and Excise receipts (by £0.2 bn, on spirits and tobacco, reflecting unprecedentedly high pre-Budget clearance from bonded warehouses), higher Inland Revenue receipts (by £0.1 bn), and lower supply expenditure (by £0.2 bn, mostly MOD procurement).

3. The LABR in April was provisionally £0.6 bn, £0.1 bn above the Budget profile, which is very close. The PCBR was provisionally a net repayment of £0.1 bn, as profiled.

4. The monthly note, presenting updated estimates for April and revised forecasts for May-July, will be circulated next Thursday. As usual we shall send you the draft press briefing at the same time.

MISS M E PEIRSON

£billion

	April 1985			April 1984
	Provisional outturn	Last month's forecast	Difference	Outturn
CGBR(O)	1.1	1.7	- 0.6	1.9
LABR	0.6	0.5	0.1	0.9
PCBR	- 0.1	- 0.1	-	- 0.4
PSBR	1.6	2.1	- 0.5	2.4

Econ 22 - X to Fowler
No reply

FROM: E P KEMP
13 May 1985

MR D M WILLIAMS

Blames

Sir PM

On index-linking, see flag X.

DB 13/5

cc Sir Peter Middleton
Mr Bailey
Sir T Burns
Mr Anson
Mr Byatt
Mr Cassell
Mr Battishill
Mr D J L Moore
Mr Monger
Mr Odling-Smee
Mr Watson
Mr Riley
Miss Seammen
Miss Sinclair
Mr G P Smith
Miss Noble
Miss Walker

FOLLOWING THROUGH "FOWLER" ETC

You had a copy of Mr Board's minute to Mr Byatt of 10 May.

2. Following up Fowler is going to involve a considerable amount of work for Supcrannuation, and I would like to have a word with you in the near future about this.

3. In no special order, and without any attempt necessarily to provide a complete list, it seems to me that the things we have got to put in hand include the following :-

a. Agreement of a form of words and briefing etc in respect of index linked public service pensions, to be used when Mr Fowler's Green Paper is published. This would follow up the Chancellor's letter to Mr Fowler, copied to Cabinet colleagues, which suggested this approach. I think you ought to be in contact with ST in the first place on this, because of course although it is Treasury business, and within Treasury Superannuation Division's business, it will have to be all part of the presumably massive briefing exercise which is being put in hand against the publication of Mr Fowler's Green Paper.

b. As part of (a), but going more widely, I think we ought to be very clear in our minds just exactly what the new dispensation is going to mean for public service pension schemes. And when we have our mind clear on this, we shall I think need to ensure that other Departments who are sponsors of or are involved in public service occupational schemes (and indeed public sector occupational schemes too) are aware of the facts of life, so that we all take a common line and all give common answers to the deluge of queries which we can I think immediately expect. It may be for this purpose you will have to hold a meeting of MOCOP, or I might even reconvene OP(PS) to make sure we are all at one.

c. Finally, and probably most difficult of all, we need to consider what we now do about carrying forward the OP(PS) work concerning on the one hand "realistic" pension contributions in line with the Manifesto and on the other making the PCSPS contributory. All this work was of course left on the back burner until after Fowler; that time has now come and we have to consider how we take things forward.

4. As I say we must have an urgent word about all this. It may be that, as I suggest, a very early meeting - before the Green Paper is published - of OP(PS) might be sensible, both by way of information, agreeing a line on publication of the Green Paper and preliminary views about how to take forward the outstanding work.

5. One strand we do not want to overlook concerns nationalised industries. As well as OP(PS) there was also set up, of course, OP(NI), which was suppose to look at index linking and all that so far as nationalised industry pension schemes went. That only had one meeting, but if index linked pensions as a subject is not going to go away for the public services, presumably it will not go away for nationalised industries etc either. We shall have to keep in touch with PE.

E P KEMP

FROM: MISS M E PEIRSON
DATE: 16 May 1985

1. MR CASSELL

2. CHANCELLOR OF THE EXCHEQUER

Copy attached for:

Mr Turnbull - No 10

cc List A	List B (distributed at 2.30 pm, 17 May)	
Sir P Middleton	Chief Secretary	Mr Peretz
Sir T Burns	Financial Secretary	Mr Mowl
Mr H Evans	Economic Secretary	Mr Stibbard
Mr Battishill	Minister of State	Mr M Williams
Mr Lankester	Mr Bailey	Mr Powell
Mr Collinson	Mr Odling-Smee	Mr Cropper
Mr Devereux	Mr Scholar	Mr Wells - CSO
Dr Webb	Mr Burgner	Mr Walton - IR
	Mr Folger	Mr Wilmott - C & E

MONTHLY NOTE ON THE PSBR

1. I attach a report on the PSBR outturn for April. This outturn will be published by press notice at 2.30 pm on Friday 17 May.

2. In this note, as usual, outturn in the latest month (April) is compared with the (Budget profile) forecast made a month ago. Forecasts for May-July are included.

3. The press notice is confined to comparisons between outturn in 1985 with outturn in 1984. As last year, in order to avoid unhelpful comparisons between one month's outturn (April) and another single month (April 1984), the press notice compares the first 4 months of calendar 1985 with the same 4 months of calendar 1984. In addition, the press briefing will warn that the normal degree of front-end-loading of the PSBR may be expected in 1985-86.

MEP

MISS M E PEIRSON

PUBLIC SECTOR BORROWING

Summary

- The PSBR for April is provisionally estimated at £1.8 billion. This is about £0.3 billion lower than last month's Budget forecast (Chart 1) and £0.6 billion lower than in April 1984 (Chart 2).

- Borrowing on central government's own account was about £0.6 billion lower than forecast while local authorities borrowed about £0.3 billion more than forecast.

- The PSBR is forecast at £2¼ billion over the next three months, to bring the total for the first four months of 1985–86 to £4 billion, close to the Budget profile.

- Revisions to the PSBR outturn for 1984–85 are small, the latest estimate remaining at £10.1 billion, or 3.1 per cent of GDP.

Figures in this report are not seasonally adjusted and also may not sum precisely because of rounding.

Chart 1 : Comparisons with Budget profiles for 1985-86

£ billion cumulative

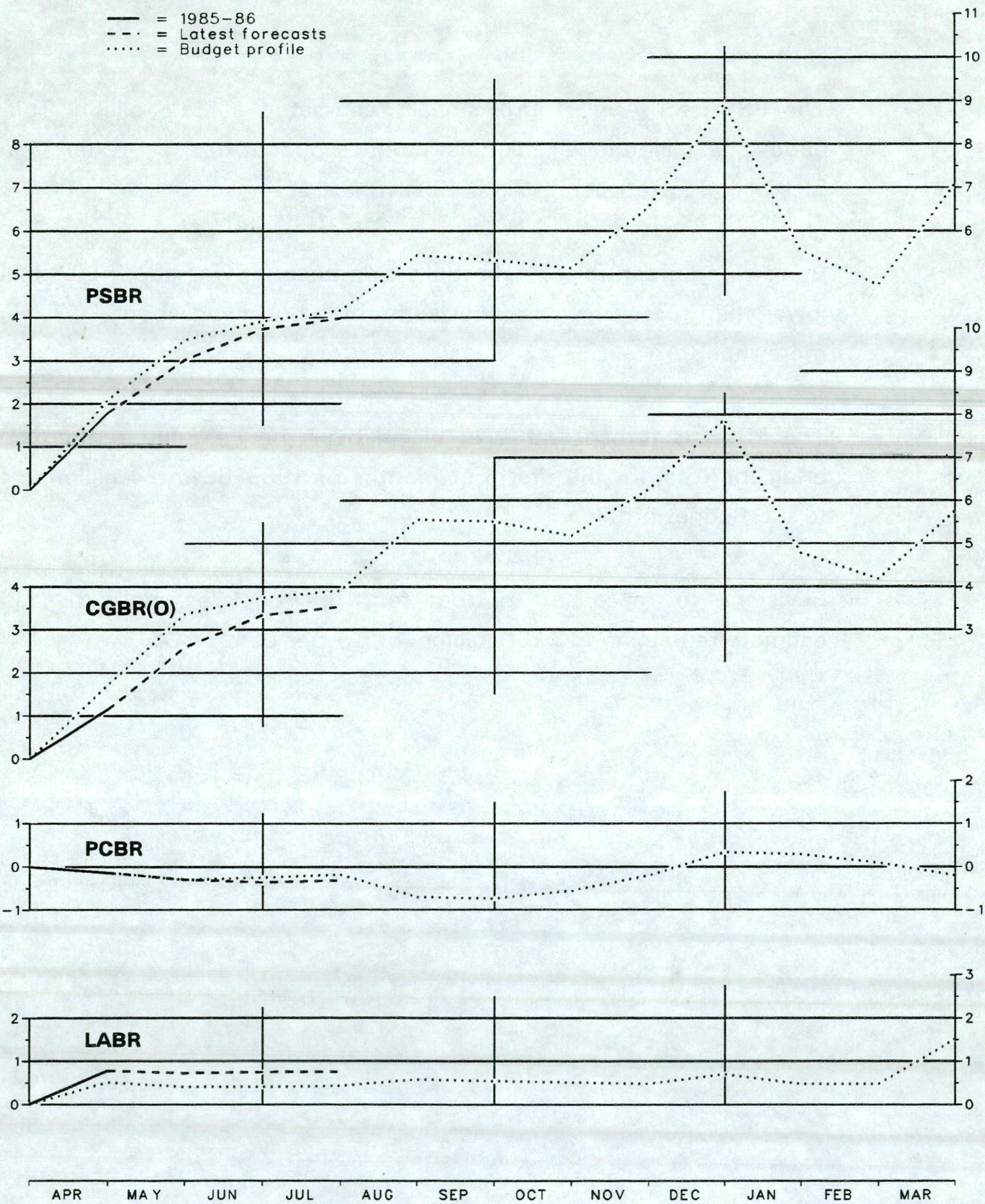
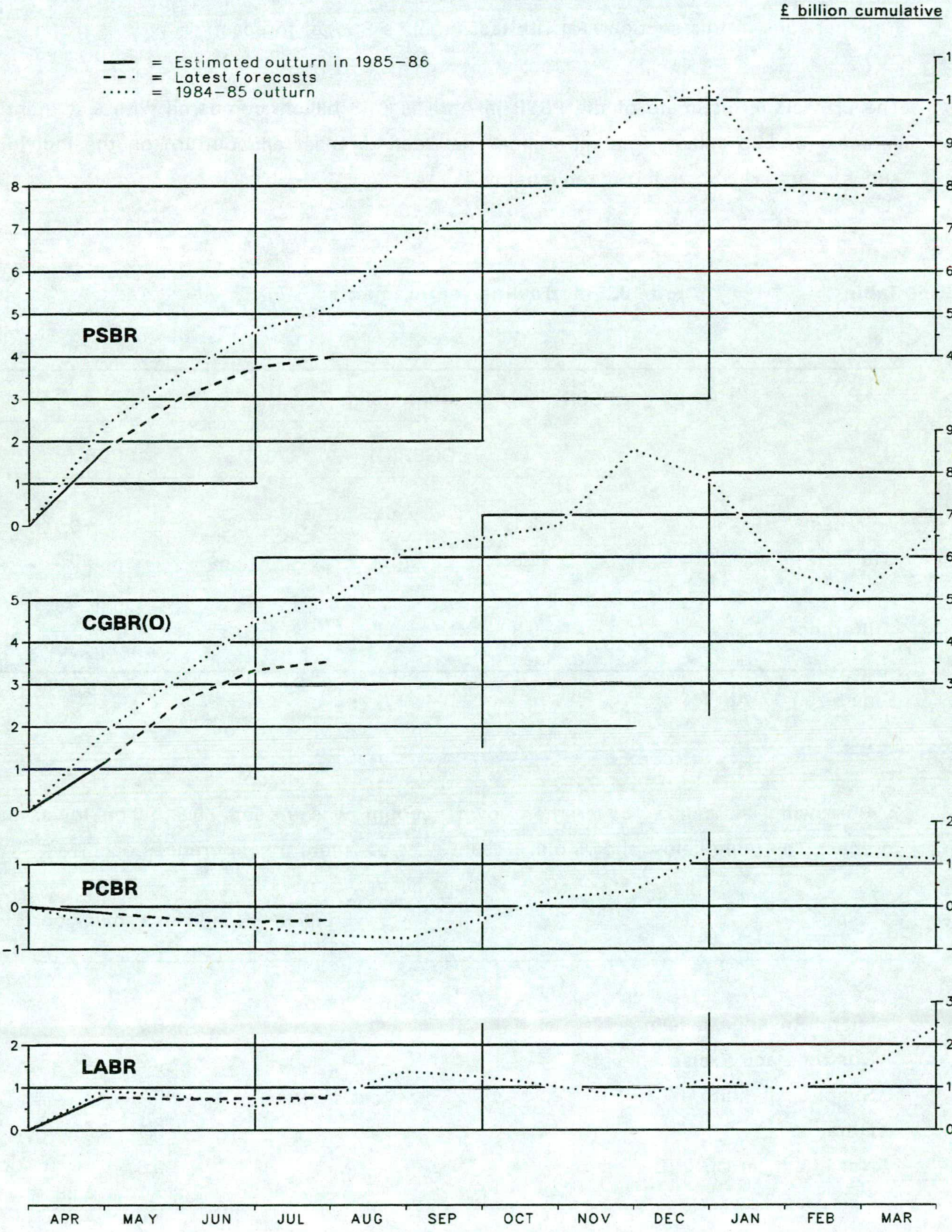


Chart 2 : Comparisons with last year's outturns



Borrowing in April

(Comparisons in this section are with last month's Budget forecast)

The provisional estimate of the PSBR in April is £1.8 billion, compared with last month's forecast of £2.1 billion. The differences between forecast and outturn on the individual sub-sectors are shown in the table below.

Table 1: April 1985 borrowing requirements

£ billion

	PSBR	Comprising		
		CGBR(O)	LABR	PCBR
Forecast*	2.1	1.7	0.5	-0.1
Outturn	1.8	1.1	0.8	-0.1
Difference	-0.3	-0.6	0.3	-

*made on 17 April

2. Borrowing on <u>central government own account</u> was around £0.6 billion lower than forecast. The table below shows our present view of where the differences occurred.

£ billion (- indicates lower borrowing)

Inland Revenue receipts	-0.1
Customs and Excise receipts	-0.2
Supply expenditure	-0.2
Other	-0.1
Net effect on CGBR(O)	-0.6

3. Higher Customs and Excise receipts were due to exceptionally large pre-Budget clearances of tobacco (and, to a lesser extent, spirits) from bonded warehouses. Lower Supply expenditure was due mainly to lower MOD procurement, and probably reflects slippage of payments to later in the year.

4. Local authorities borrowed £0.8 billion in April, about £0.3 billion more than forecast last month. We have no information on the reason for the difference. With the change in the capital control system coming into force on 1 April 1985, it may be that authorities spent more heavily than expected at the end of March and that some associated borrowing spilt over into April. (That happened in March/April 1984, when borrowing in April was £0.9 billion). The rate-capped authorities borrowed rather less than is usual in April, so the high borrowing was not due to the delays in setting rates.

5. Public corporations made a net repayment of debt of £0.1 billion in April, as forecast last month.

May to July

6. The PSBR in the period May to July is forecast to be £2¼ billion, bringing the total for the first four months of 1984-85 to £4 billion, close to the Budget profile.

7. Table 4 shows the latest detailed profile of borrowing on central government own account for April to July; a comparison with the Budget forecast for the first four months and the outturn in April-July 1984 is provided in Table 5.

8. Borrowing in the next three months, in total, is forecast slightly higher than in the Budget profile, as some of the factors which led to the lower borrowing in April (principally Customs and Excise receipts) are expected to unwind.

9. Forecast Supply expenditure over these three months is below the expected average for the year, but tax receipts are also lower than average (with the exception of Inland Revenue receipts in July). Asset sales are high in June.

- In May, the CGBR(O) is forecast to be £1½ billion. Cyclically high VAT receipts are offset by lower receipts of tobacco duty following the large clearances from bonded warehouses in April. The sale of British Aerospace is expected to raise about £0.2 billion from the first call in May.

- In June, the CGBR(O) is forecast to be £¾ billion. The second call on BT shares will raise £1¼ billion. Debt interest payments are relatively low.

- In July, the CGBR(O) is forecast to be only £¼ billion. Inland Revenue receipts are high, including the second instalment of Schedule D tax from the self-employed (£1 billion), quarterly advance corporation tax (£½ billion) and first payment of banks' composite rate tax (£¼ billion). Asset sales are assumed to raise £½ billion.

10. Local authorities are expected to make a small net repayment of debt over the next three months, as in the Budget profile. There are no grounds for assuming that the higher borrowing in April will be offset by higher net repayment in the following months.

11. Public corporations are also expected to make a small net repayment over the next three months, accounted for by the Electricity Supply and Gas industries, much as in the Budget profile.

1984-85

12. The estimate for the PSBR outturn for 1984-85 remains £10.1 billion, or 3.1 per cent of GDP.

Table 2: Borrowing Requirement monthly profiles May-July

£ billion

	PSBR	Comprising		
		CGBR(O)	LABR	PCBR
1985-86				
Apr	1.8	1.1	0.8	-0.1
May	1.2	1.4	-0.1	-0.2
Jun	0.7	0.7	-	-0.1
Jul	0.2	0.2	-	-
Cumulative				
Apr	1.8	1.1	0.8	-0.1
May	3.0	2.6	0.7	-0.3
Jun	3.7	3.3	0.8	-0.4
Jul	4.0	3.5	0.8	-0.3

Figures for April are outturns

Table 3: PSBR for 1985-86 - Comparisons with 1984-85 and Budget profile

£ billion

	1984-85	1985-86		Differences from	
	Outturn	Budget profile	Latest update[1]	1984-85 outturn	Budget profile
	1	2	3	3-1	3-2
Apr	2.4	2.1	**1.8**	-0.6	-0.3
May	1.2	1.4	**1.2**	-	-0.1
Jun	1.0	0.4	**0.7**	-0.3	0.3
Q2	4.6	3.9	**3.7**	-0.9	-0.2
Jul	0.6	0.3	**0.2**	-0.3	-
Aug	1.6	1.3			
Sep	0.6	-0.1			
Q3	2.8	1.4			
Oct	0.6	-0.2			
Nov	1.7	1.4			
Dec	0.7	2.4			
Q4	2.9	3.6			
Jan	-2.4	-3.4			
Feb	-0.2	-0.8			
Mar	2.4	2.3			
Q1	-0.2	-1.8			
Cumulative					
Apr	2.4	2.1	**1.8**	-0.6	-0.3
May	3.6	3.5	**3.0**	-0.6	-0.5
Jun	4.6	3.9	**3.7**	-0.9	-0.2
Jul	5.2	4.2	**4.0**	-1.2	-0.2
Aug	6.8	5.4			
Sep	7.4	5.3			
Oct	8.0	5.1			
Nov	9.7	6.5			
Dec	10.3	8.9			
Jan	7.9	5.6			
Feb	7.7	4.8			
Mar	10.1	7.1			

[1]Figures for April are outturns

Table 4: Central government transactions - April outturn and latest forecasts for May-July

£ billion

	April		Latest forecasts		
	forecast	outturn[1]	May	Jun	Jul
Receipts					
Consolidated Fund					
Inland Revenue	3.7	3.8	3.7	3.1	5.3
Customs and Excise	3.1	3.3	2.9	2.4	2.8
Other[2]	0.6	0.4	1.4	1.7	1.3
National Loans Fund					
Interest etc. receipts	0.5	0.6	0.5	0.5	0.4
Total Receipts	8.0	8.1	8.3	7.8	9.8
Expenditure					
Consolidated Fund					
Supply expenditure[3]	8.3	8.1	7.6	7.5	7.9
Adjustment to Supply Services basis[4]	-	0.3	-	-	-
Other	0.3	0.3	0.3	0.3	0.3
National Loans Fund					
Service of the national debt	1.0	0.9	1.6	0.5	1.8
Net lending	0.1	0.1	-	0.3	0.4
Total Expenditure	9.6	9.7	9.5	8.6	10.4
Other funds and accounts (+ increases borrowing) (- reduces borrowing)	0.2	-0.7	0.6	0.2	-0.1
CGBR	**1.9**	**0.9**	**1.7**	**1.1**	**0.6**
On-lending	0.1	-0.2	0.3	0.3	0.4
CGBR(O)	**1.7**	**1.1**	**1.4**	**0.7**	**0.2**

(1)Due to time lags in some items reaching their final accounting destination, figures of forecast and outturn may not be strictly comparable for the components identified, but there is no effect on the overall CGBR.
(2)Includes National Insurance Surcharge and receipts from sales of assets
(3)On a cheques issued basis. Supply includes an element of on-lending in the form of public dividend capital etc.
(4)Reflects changes in balances of departmental accounts with the Paymaster General, timing and other differences between cheques issued by departments and payments to them from the Consolidated Fund. An offset to this item is included in "Other funds and accounts".

Table 5: Central government transactions[1] – comparisons for April–July

£ billion

	1984	1985	
	Outturn	Budget forecast	Latest update
Receipts			
Consolidated Fund			
Inland Revenue	14.1	15.8	15.8
Customs and Excise	10.4	11.3	11.3
Other[2]	3.5	5.0	4.8
National Loans Fund			
Interest etc. receipts	1.5	1.9	2.0
Total Receipts	29.5	34.0	33.9
Expenditure			
Consolidated Fund			
Supply expenditure[3]	29.2	31.6	31.1
Adjustment to Supply Services basis[4]	–	–	0.3
Other	1.7	1.2	1.3
National Loans Fund			
Service of the national debt	4.3	4.8	4.9
Net lending	-0.1	1.0	0.7
Total Expenditure	35.1	38.6	38.2
Other funds and accounts (+ increases borrowing) (- reduces borrowing)	-0.3	0.4	-0.1
CGBR	**5.4**	**5.1**	**4.3**
On-lending	0.4	1.1	0.8
CGBR(O)	**5.0**	**3.9**	**3.5**

(1)Due to differences in treatment of some items in the accounts between the periods/forecasts shown, and time lags in some items reaching their final accounting destination, figures for the components identified may not be strictly comparable.
(2)Includes National Insurance Surcharge and receipts from sales of assets.
(3)On a cheques issued basis. Supply includes an element of on-lending in the form of public dividend capital etc.
(4)Reflects changes in balances of departmental accounts with the Paymaster General, timing and other differences between cheques issued by departments and payments to them from the Consolidated Fund. An offset to this item is included in "Other funds and accounts".

C./ Press notice goes out at 2:30 pm tomorrow. Content with Q and As?

Rwo 16/5

FROM: MISS M E PEIRSON
DATE: 16 May 1985

PPS/CHANCELLOR

cc Mr Cassell

MONTHLY NOTE ON PUBLIC SECTOR BORROWING, AND PRESS BRIEFING

1. Later today I will send the latest monthly note on the PSBR to the Chancellor. As usual, it will be accompanied by an additional copy for you to forward to No 10.

2. A covering letter for you to send to Andrew Turnbull is attached. The note should reach No 10 this evening.

3. I also attach the draft press briefing. The aim is to circulate it to List A recipients by 10.30 am tomorrow. (List A has been expanded to include all Treasury Ministers, as noted in Mr Board's minute of 7 May.) Any comments which the Chancellor might have can be taken on board provided you can let Mr Clark (ext 3093) have them before 9.30 am tomorrow, and earlier if possible.

MEP

MISS M E PEIRSON

SECRET

38/28

FROM: MS D J SEAMMEN

DATE: 17 May 1985

SIR P MIDDLETON

cc Mr Bailey
Sir T Burns
Mr Anson
Mr Cassell
Mr Kemp
Mr Battishill
Mr Monger
Mr Odling-Smee
Mr Watson
Mr Byatt
Mr Riley
Mr G P Smith
Mr D M Williams
Miss Noble
PS/Inland Revenue
Mr Isaac - I/R

(1) Same green paper
(2) No time. Thursday (seen written)
(3) No fgs for Ec analysis
(4) Nothing on transit protection
(5) Invalidity (insurance)

FOWLER REVIEWS: SERPS

You asked to be brought up to date on progress.

2. DHSS have been fully involved with their Ministers all this week. At a meeting with them today we went through all they had to offer, which was an oral account of the features of the compulsory scheme, to be written up in the Green Paper. I attach a summary. Thinking has not advanced very far over there, and on key issues of administration there is no progress.

PK having a meeting ✓

3. On the implications of the compulsory scheme for public service schemes, and public sector schemes, Mr Kemp intends to be in touch with DHSS direct. He will in particular want to note DHSS intentions for the Green Paper on the subject of post-award indexation. For presently contracted out schemes in particular, this gets no more clear.

4. DHSS were not ready to report on the scheme for transitional protection for the under 50s.

5. Nor were they ready with any Green Paper drafts on the phasing out of SERPS over the 3 year period; we indicated that in our view there must be, on an illustrative basis,

an indication of the changes in contribution rates for various categories between 1987-88 and 1989-90.

6. DHSS are now worrying about invalidity benefit, and in particular the contrast between the over 50s (who will retain rights to earnings related invalidity benefit) and the under 50s who will not (apart from accrued rights). There are of course no proposals for compulsory insurance against long term disability. We emphasised that we would need to see their proposals in good time. While they would not be included in the Green Paper, questions would be asked very soon thereafter.

7. This brings us to timing. If the Green Paper is to be published in the week of the 3 June, it needs to go for printing by Thursday next week. Mr Watson emphasised that we should need to see drafts of the Green Paper, with full supporting documentation, in good time and the Chancellor himself would no doubt require at least 48 hours. On this basis, 3 June seems an unlikely target date. But the uprating statement in the week of 17 June imposes a date beyond which we cannot slip without severe embarrassment.

DJS

MS D J SEAMMEN

Nong

Vhalf baked

FEATURES OF A COMPULSORY SCHEME

Coverage

(i) Everyone above the LEL will be included; there will be some (not as yet worked out) averaging system to exclude those with occasional earnings above the LEL.

(ii) the age for entry will be 18;

(iii) presently opted out married women will be included;

(iv) there will be no waiting period (so all casuals will be included)

(v) self employed will not be covered.

Pension Providers

(i) Only companies in the business of insurance will be able to provide annuities;

(ii) but "money boxes" will include "Banks, Building Societies, Unit Trusts and Merchant Banks" we queried the omission of Stockbrokers;

(iii) Mr Fowler is seeing Mr Tebbit about aspects of investor protection including,

(a) possible reserve powers to prescribe the range of investments;

(b) the possibility of a compensation fund;

(c) the proper regulatory framework for self-administered schemes;

(iv) no restrictions are at present enivsaged on commissions, marketing practices etc;

(v) it is expected that at least some of the above will go into the forthcoming Gower Bill.

Contributions

(i) DHSS propose that the Green Paper should illustrate the effect of contributions at 4%, 5% and 6% of earnings; the Treasury emphasised that in any range 4% must be the central figure.

(ii) DHSS proposed that the question of a UEL for compulsory contribution should be left open in the Green Paper; Treasury said that in our view it should propose a UEL, while leaving the point open for consultation.

Indexation

(i) The Green Paper would propose 3 options

(a) 5% or prices, whichever was less;

(b) 3% flat (irrespective of prices);

(c) no indexation.

(ii) there would eventually have to be an indexation requirement (one of the above) for existing contracted out schemes (which would qualify automatically); but for a period there might not be such a requirement, given the better pensions overall payable under existing contracted out schemes; this area would be vague in the Green Paper.

Commutation

(i) DHSS propose that the Green Paper should not say that there would be no commutation from the minimum pension (although this was the intention); Treasury said this should be spelled out in the Green Paper.

(ii) DHSS thought this might imply some restriction on existing commutation provisions, but this was unclear.

(iii) they had not turned their minds to tax provisions and we did not remind them.

Survivors

(i) Some provisions would be necessary for benefits for death in service, but DHSS had no particular proposals - perhaps lump sums;

(ii) for death after retirement, half the pension would pass to the widow or widower.

Pension age

(i) The Green Paper would make clear that pensions would be payable by age 65 for both men and women;

(ii) it would suggest that they might be available for either sex from age 60 on an actuarially reduced basis; Treasury pointed out that earlier discussions on this subject had thought there would need to be a reverse means test, to ensure that people did not fall back on supplementary benefit; DHSS thought this would not be applicable to private schemes;

(iii) the Green Paper would float unisex annuity tables; this would fit in with the equalisation of pension age; in the context of money purchase schemes, this would favour women, but thisadvantage would be reduced by equality of survivors benefits.

Personal pensions

(i) The Green Paper would not deal with the possibility of people opting back into employers' schemes in middle age; the thought was that schemes could please themselves on this;

(ii) the Green Paper would say that optants for personal pensions would have no ability to take accrued rights before A day but would be vague about the possibility of transfer into personal pensions of future accrued rights;

(iii) Treasury pointed out that both the above would have implications for public service pensions.

Additional voluntary contributions

Qualifying schemes must offer this facility.

Occupational Pensions Board

DHSS saw its existing role continuing much as before; Treasury pointed out it would be necessary to pick up the recommendations of the Rayner scrutiny of the SFO/OPB.

Clearing house

(i) DHSS offered no further thinking on this; it was thought that some kind of "Sorting House" would be required but the clearing house might not deal with money;

(ii) Treasury pointed out that some kind of a clearing house was essential to the operation of the scheme; not least because Inland Revenue would require consolidated information from it in order to operate the tax rules.

From: JOHN CLARK
XX May 1985

MR CULPIN - IDT

MR LANG - CSO Press Office

cc List A

Chancellor
Chief Secretary
Financial Secretary
Economic Secretary
Minister of State
Sir P Middleton
Sir T Burns
Mr Cassell
Mr H Evans

Mr Lankester
Mr Collinson
Mr Folger
Miss Peirson
Mr Peretz
Mr R Evans
Mr Ward - CSO
Mr Wright - B/E
Mr Turnbull - No. 10

List B
(distributed at 2.30pm, 17 May)

Mr Stibbard
Mr Spencer
Mr Cropper
Mr Lord
Mrs Hillier - IR
Mr D Mitchell - C and E

DRAFT BRIEFING FOR 17 MAY PSBR PRESS NOTICE

The PSBR figures for April will be published at 2.30pm on 17 May. The provisional outturns, together with figures for the first four months of 1984 and 1985, are shown in Table 1. Cumulative figures for the PSBR and its components for 1984-85 and 1983-84 are shown in Table 2 overleaf.

Table 1: Borrowing requirement outturns

£ billion

	Jan-Apr 1984	Jan-Apr 1985	April 1985
Central government on own account	1.0	-0.1	**1.1**
Local authorities	2.1	2.0	**0.8**
Public corporations	-0.7	-0.3	**-0.1**
PSBR	2.3	1.6	**1.8**
Memo: CGBR (including borrowing for on-lending to LAs and PCs)	1.9	0.9	**0.9**

Note: Figures may not sum precisely because of rounding.

Table 2: **PUBLIC SECTOR BORROWING REQUIREMENT - Comparison with the last two years**

Cumulative £ billion

	Central government on own account			Local authorities borrowing requirement			Public corporations borrowing requirement			Public sector borrowing requirement		
	1983-84	1984-85	1985-86	1983-84	1984-85	1985-86	1983-84	1984-85	1985-86	1983-84	1984-85	1985-86
Apr	0.9	1.9	**1.1**	0.5	0.9	**0.8**	-0.2	-0.4	**-0.1**	1.2	2.4	**1.8**
May	2.4	3.2		0.3	0.8		-0.3	-0.4		2.4	3.6	
Jun	3.7	4.5		-0.1	0.6		-0.4	-0.5		3.2	4.6	
Jul	4.5	5.0		-0.0	0.8		-0.6	-0.7		3.9	5.2	
Aug	5.7	6.2		0.3	1.4		-0.4	-0.7		5.6	6.8	
Sep	6.6	6.4		0.3	1.2		-0.0	-0.3		6.9	7.4	
Oct	6.7	6.8		0.3	1.0		0.1	0.2		7.1	8.0	
Nov	8.3	8.6		-0.2	0.8		0.4	0.4		8.5	9.7	
Dec	9.1	7.9		0.1	1.2		0.6	1.3		9.8	10.3	
Jan	6.3	5.7		0.1	0.9		0.7	1.3		7.1	7.9	
Feb	6.7	5.1		0.2	1.3		0.6	1.2		7.5	7.7	
Mar	8.2	6.5		1.2	2.4		0.3	1.1		9.7	10.1	

Note: Figures may not sum precisely because of rounding.

CONFIDENTIAL AND PERSONAL
(DRAFT)

2. The (provisional) PSBR for April is £1.8 billion. This is in line with the average of forecasts of City analysts, which are for borrowing of between £1½ billion and £2¼ billion in April.

3. The April outturn is £0.6 billion lower than April 1984 and £0.6 billion higher than April 1983, although it should be stressed that comparisons over a period of months are more useful (Table 1).

4. The Q and A briefing below gives background and sets out the line to take on particular issues.

Q1. Comment on April PSBR?

Line to take

Provisional outturn ~~close to average April PSBR of last two years.~~ £0.6 billion lower than April 1984 PSBR. No special factors affected borrowing in the month. Borrowing in first four months of calendar 1985 £0.7 billion lower than in corresponding period of 1984.

Q2. How much of the 1985-86 PSBR is expected in the first half-year?

Background

Last year Chancellor said "almost all" of PSBR in 1984-85 was expected in first half of year; such high front-end loading was expected because of special receipts in second half of year (VAT on imports and BT). But the prolongation of the coal strike added substantially to borrowing in the second half, so in the event no more than three-quarters of the PSBR was in the first half-year. In 1985-86, BT second call receipts (June) will reduce borrowing in the first half-year, but higher corporation tax receipts (than in earlier years) will reduce borrowing in the second half-year, so on balance no reason to expect front-end-loading to be very different from past average.

Line to take

Although very uncertain at this stage, no reason to suppose that proportion of borrowing in first half-year will be very different from usual (around two-thirds). British Telecom second call receipts will benefit PSBR in first half of 1985-86, but higher corporation tax receipts (than in earlier years) will principally benefit second half.

Q3. Any effect of miners' strike on PSBR in April/1985-86 ?

Line to take

The only directly identifiable effect in April was some slippage of miners back holiday pay from 1984-85. This will be taken into account in reviewing NCB's EFL (PEWP figure was stated as provisional), but any increase would come from the £5 billion Reserve.

Q4. Asset sales?

Line to take

No significant receipts from special sales of assets in April. First instalment of receipts from sale of British Aerospace shares (nearly £0.2 billion gross) due in May, second instalment due in September. Second instalment of BT receipts (about £1¼ billion) due in June. Budget forecast for 1985-86 £2.5 billion.

Q5. Supply Expenditure in April?

Background

At £8.6 billion, supply services (which represents issues to departments from the Consolidated Fund) were 10.6 per cent higher than in April 1984. The comparable increase in supply expenditure (which represents cheques issued by departments and differs from supply services because of changes in departmental balances with the Paymaster General) is about 3½ per cent. The latter figure is not published and is based on less firm information. No Budget forecast of supply in 1985-86 was included in the FSBR. Table 5.3 showed Main Estimates provision only, which is unsuitable for comparing against outturn.

Line to take

Supply expenditure is seasonally high in April. Much too early in year to draw conclusions from the figure - cannot read much from one month's outturn. In any case, figures for supply services do not take account of changes in departmental balances. The increase in actual supply expenditure is much less than 10½ per cent (although the estimate for this is less firm than for supply services).

Q6. EC refunds?

Line to take

Whole of 1983 refund received in 1984-85. 1984 refund of 1000m ecus (about £¾ billion at present) expected in late 1985-86. 1985 arrangements are different, and will reduce UK monthly contributions, starting in 1986.

Q7. Inland Revenue receipts in April?

Background

Total Inland Revenue receipts 12.7 per cent up on April 1984. Budget forecast for 1985-86 was for receipts of £56.2 billion, up 11.6 per cent on 1984-85.

Line to take

Inland Revenue receipts in April were £3.8 billion. Little can be read from one month's figures.

Q8. Customs and Excise revenues?

Background

Customs and Excise revenues were 34 per cent higher than in April 1984. Budget forecast for 1985-86 was for receipts of £36.3 billion, up 2¼ per cent on 1984-85 (low increase because 1984-85 receipts were boosted by change in VAT on imports).

Line to take

Receipts in April were £3.3 billion. They were boosted by high pre-Budget clearance of tobacco and alcohol from bonded warehouses, some continued effect of the change in VAT on imports, and other factors. Little can be read from one month's figures.

Q9. Local authorities' borrowing?

Background

Preliminary estimate is that local authorities borrowed £0.8 billion in April. Budget forecast for 1985-86 as a whole £1.5 billion. Outturn above April average for last few years, but below outturn for April 1984.

Line to take

Local authority borrowing in April is normally high, because of seasonally low rate income.

Q10. Public corporations' borrowing?

Background

Public corporations made a net repayment of debt of £0.1 billion in April (provisional). Budget forecast for 1985-86 as a whole is for a net repayment of £0.2 billion.

Line to take

Public corporations have shown a net repayment of debt in April in each of the last 3 years.

John Clark (ext 3093)
PSF Division, HM Treasury

016/104

Mr Cassell

PPS
Mr Bailey
Sir P Middleton
Mr Byatt
Mr Watson
Ms Seammen
Ms Noble
Mr Scholar
Mr Cropper
Mr Lord.

CHIEF SECRETARY TO THE TREASURY

Treasury Chambers, Parliament Street, SW1P 3AG

Rt Hon Norman Fowler MP
Secretary of State
Department of Health and Social Security
Alexander Fleming House
Elephant and Castle
London
SE1 6BY

21 May 1985

Dear Secretary of State

SOCIAL SECURITY REVIEWS

I understand from my officials that drafts of several important sections of your Green Paper are not yet available. I do not want to delay publication. But there are a number of points where it is crucial that we get ourselves organised properly to make the Green Paper a success.

I am particularly anxious to see as quickly as possible the revised sections of the Green Paper dealing with our pension proposals. These will have to cover a considerable amount of ground, including the proposed arrangements for compulsory private pensions, the revised proposals for transitional protection for those under 50 and the associated NIC proposals. Much of this material will be new. It is essential that we get it right. That means having a clear and agreed understanding of all the supporting costings and analysis of the economic implications.

I also think it is essential that we agree well in advance of publication the line we propose to take in public about all the major changes proposed in the Green Paper. There are a number of loose ends that need tidying up, including the treatment of invalidity benefit. We cannot put together effective and convincing statements of the case for our proposals until we see drafts of the Green Paper itself. Our officials will also need to agree on the detailed analysis, for example of winners and losers, which must underlie effective briefing. I was extremely concerned to hear that there has been no further discussion of these issues at official level since we met earlier this month.

I am copying this letter to the Prime Minister.

Yours sincerely

J Broadbent

for PETER REES

[Approved by the Chief Secretary]

Sir PM

28 MAY 1985

FROM: E P KEMP
DATE: 28 MAY 1985

CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Sir Peter Middleton
Sir Terence Burns
Mr Bailey
Mr Anson
Mr Scholar
Mr Watson
Miss Seammen
Mr D Williams
Mr Gilhooly
Miss Noble
Mr Cropper
Mr Lord

SOCIAL SECURITY REVIEWS - PUBLIC SERVICE PENSIONS

Mr Fowler's letter to you of 20 May replies to yours of 22 April.

2. Mr Fowler agrees with you on the line to take on indexation of public service pensions. In effect, this remains as in the Manifesto; full price protection remains "on the basis of realistic contributions". We are working with DHSS on a public line to take when the green paper appears. Almost certainly questions will come up, so we shall have to say that the "realistic contribution" dimension is still open, albeit in abeyance while the Fowler reviews were on. We shall put you further advice on how this matter might be taken forward when the green paper is out and we see what reactions emerge on this point.

3. Mr Fowler also agrees that public service pension schemes may have to be amended to bring in part-timers, but notes (correctly) that the estimated costs of this have been taken into the arithmetic. In practical terms this may give some tricky problems for public service employers and public service pension schemes, but then so it will for others also.

4. Mr Fowler in his letter takes the chance of picking up the point you raised earlier (as recorded on the second page of the No 10 record of the meeting held on 6 May); namely whether personal pensions should be available in the case of unfunded public service schemes. It was left that you would discuss this further with the Secretary of State for Social Services. Mr Fowler makes it clear that he thinks that personal pensions should be available in these cases; indeed he thinks that personal pensions should be available to all.

5. One can see why Mr Fowler wants public service schemes included. If personal pensions are a good thing socially and economically, then it is difficult for the Government to argue that the public service and public service employees should be left out. Leaving out such a large group of people would encourage other employers to look for exemption. In any case, Mr Fowler says, in practice members of public service schemes are unlikely to see advantage in choosing a personal pension.

6. We would in fact prefer the public service schemes were left out. Notwithstanding what Mr Fowler says about the point being academic, some people in the public services will probably take a personal pension (eg young nurses who only intend to stay for a very few years), and this gives a short-term cost; if 1 per cent of the pay bill took the option and 4 per cent employer/employee contribution had to be paid to the provider of the personal pension, I estimate the cost would perhaps be £8 million per annum - this is of course very small in the totals, and anyway there ought to be a long-term saving if this meant that some people contented themselves with the minimum contribution and did not seek one way or another to get the rest of the employer/contribution But it is still all in the wrong direction, and of course more than 1 per cent could opt. More importantly, if less tangibly, there could be upward pressures on pay, especially in non-contributory schemes, if people seek to take out by way of pay what they see the employer

as having saved by their leaving his scheme and going into a personal scheme. A civil servant, for instance, might point to the fact that the current overall contribution rate is put at 20 per cent, of which he is deemed to "pay" around 8 per cent by this being built into his salary rate; he might say that he is in some way entitled to the balance of 16 per cent which emerges after the employer has paid over 4 per cent.

7. On the whole, I do not think you would win an argument with Mr Fowler about coverage of the personal pension scheme. Indeed Mr Fowler will argue that he has come to meet you by (1) not suggesting that the <u>whole</u> of the present personal pension contribution (employee plus employer) should go to the personal pension provider - as the personal pensions lobby will undoubtedly argue - but only 4 per cent; and (2) not allowing back-dating before the starting date of the new legislation and leaving open the question of back-dating thereafter. So while from my perhaps limited point of view I cannot be very happy, I think we probably have to go along. It is worth noting, of course, that upward pressures on pay, on the lines I have sketched out, could arise throughout the economy and not just in public service schemes. We (and other employers) will just have to try resist these pressures; this will be a factor to take into account when we return to the work on realistic contributions etc referred to in my paragraph 2 above, since this will have to look also at whether or not the PCSPS stays non-contributory and aspects of the financing of public service schemes.

8. We may yet find Mr Heseltine arguing that the Armed Forces pension scheme should be exempted. This is his earlier position However MOD tell us that it now seems more likely that provided (1) and (2) of my previous paragraph obtained, he is likely to go along with Mr Fowler's line that there should be no exemptions. We shall see his letter very shortly. If Mr Heseltine does want to continue to argue the point, then there

will be some serious thinking to be done; since there is no particular reason why the Armed Forces pension scheme, and indeed the Armed Forces, are very different from many other public service employees.

9. Mr Fowler's letter to you of 20 May does not seem to call for a reply, provided you are content with the line above. We are working with DHSS officials and officials of other departments to put together a public line, including answers to the sort of questions which public service employers, employees and unions will raise, for use after publication of the green paper.

E P KEMP

31 MAY 1985

Sir PM

BF 3/6

MINISTRY OF DEFENCE WHITEHALL LONDON SW1A 2HB

TELEPHONE 01-218 9000

DIRECT DIALLING 01-218 2111/3

MO 4/6/2

29th May 1985

30 MAY 1985

Ms SEAMMEN
CST FST MST EST
SIR P MIDDLETON
SIR T BURNS
MR BAILEY MR KEMP MISS NOBLE
MR ANSON MR DWILLIAMS MR CROPPER
MR LORD

Dear Secretary of State

SOCIAL SECURITY REVIEW: PUBLIC SERVICE PENSIONS

Thank you for sending me a copy of your letter of 20th May to Nigel Lawson.

We have discussed this matter informally. As I understood what you were saying the Armed Forces would not be included in the proposed personal pension arrangements if that necessitates the Armed Forces Pension Scheme becoming directly contributory. That would almost certainly add £25 million a year to the Defence Budget at current prices, and the figure could rise to £45 million. There is obviously no point in accepting this level of additional expenditure simply to offer Servicemen a choice that few, if any, would regard as a real extension of opportunity.

I am prepared, while maintaining the present arrangement whereby the Armed Forces Pay Review Body deducts 11% from comparator pay in respect of the full excess of benefit of the Armed Forces Pension Scheme over comparator schemes, to offer the choice of a personal pension to Servicemen on the basis that my Department will contribute to that pension both the minimum employer's and employee's contributions of 2% each with the Serviceman relinquishing any claim to occupational pension scheme benefits accruing from the date of the option. There is, of course, a presentational difficulty

The Rt Hon Norman Fowler MP

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in offering such a one-sided choice - and the Armed Forces will not be alone in that - and for that reason I see considerable merit in good occupational pension schemes being exempt from the requirement to offer a personal pension to their existing members. To my mind it is easier to defend no choice at all than a completely bogus choice.

If, however, you maintain your present policy that all occupational pension scheme members should, without exception, be offered the choice of a personal pension, then I am sure that we shall in the coming months come under considerable pressure to explain why, if the Government is so committed to personal pensions, there is not a requirement on employers to fund them to the same level of contribution as they currently fund, or notionally fund, occupational pensions. If that were conceded, however, and extended to the public services, there could be a considerable adverse effect on public expenditure in the short term, even if neutral in the longer term. It will be important, therefore, rigidly to maintain the minimum contribution requirement of 4%; and in no circumstances to require public service pension schemes to fund personal pensions over and above that amount.

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

Michael Heseltine

(Approved by the Secretary of State and signed in his absence)

Sir PM

From: J ODLING-SMEE

31st May 1985

SIR PETER MIDDLETON

cc Sir Terence Burns
Mr Byatt
Mr Mowl
Mr Riley
Ms Seammen
Mr Hood
Mr Spencer
Mr Short
Mrs Holmans

ECONOMIC EFFECTS OF COMPULSORY PRIVATE PROVISION OF PENSIONS

I had hoped to be able to send you our final report on this today in preparation for the publication of the Green Paper on Monday. Unfortunately, it has taken us longer than I expected to carry out the analysis. I am hoping to circulate the report next week. The broad argument and most of the numbers in the attached draft are unlikely to change, but there is room to make it more readable. You might therefore like to wait for the next version before reading it.

2. I shall reply to the questions you raised in your minute of 15th April when the final report is circulated.

X

JOS 01

J ODLING-SMEE

I look forward to X because having read paras 23 et seq I still do not see why the total level of savings and investment in the economy will be higher. If income incomes are held constant and markets operate perfectly Does this not mean the transition from unfunded part has to be fully offset. I can't see why there should be this effect. And I cannot see why ~~was~~ a tendency for saving to increase should be a reason for reducing the growth of money GDP. P

THE MACROECONOMIC EFFECTS OF THE GREEN PAPER PENSION PROPOSALS

The Green Paper proposes a gradual phasing out of the State Earnings Related Pension Scheme (SERPS) and its partial replacement by private penson arrangements. This paper provides an economic analysis of these proposals.

2. The first section reviews the existing SERPS arrangements and the implications which these would have for the future burden of pensions. The second outlines the Green Paper proposals, their likely macroeconomic consequences and their policy implications. Section III looks at the long-term benefits of the proposed arrangements in more detail and attempts to quantify some of the more obvious effects. The quantitative analysis is described further in an annex. The final section uses the Treasury model to analyse the impact which the proposals are likely to have over the first five years of their operation.

I. THE EXISTING SERPS ARRANGEMENTS

3. The state earnings-related pension scheme (SERPS) which came into being in 1978 was set up to ensure earnings-related pension benefits for all NI contributors. Because of the desire to encourage partnership between the existing private schemes and the state scheme, contracting-out arrangements were set up to allow occupational schemes to join in the provision of earnings-related pensions at the level considered suitable for state earnings-related provision. The State would either provide earnings-related benefits directly to NI contributors through SERPS or indirectly, by contracting-out the earnings-related element of state pensions to occupational schemes for them to provide, in return for the payment of a rebate on their NI contributions. The rebate was calculated by GAD, on the basis of a $2\frac{1}{2}$ per cent real rate of return, as (roughly) the actuarial amount (as a percentage of relevant earnings) necessary to fund the "guaranteed minimum pension" (GMP). This relationship between the State National Insurance Fund, financed on a PAYG basis, and funded occupational pension schemes makes the macro-economic analysis of the present system and the possible effects of its abolition very complex.

1. Pension Provision under SERPS for contracted-in and contracted-out members

4. The complexity of the relationship between the National Insurance Fund and occupational pension schemes within the present SERPS arrangements often leads to confusion when considering future benefits under SERPS. It is not generally realised that contracted-out NI contributors are members of SERPS and would receive state benefits under these arrangements. On present GAD projections about half of the expenditure from the NI Fund on earnings-related pensions will ultimately go to people who have had periods of contracted-out employment and their surviving spouses. This is due to the arrangements between the State and the occupational schemes, whereby the latter fund GMPs up to the point of award, and the NI Fund thereafter bears the cost of bringing the GMPs up to the level of the equivalent state earnings-related pension paid to full contracted-in members, and of inflation-proofing during the subsequent period of payment.

5. A full contracted-in SERPS member who has paid NI contributions for at least 20 years receives an earnings-related pension when he retires, equal to 25 per cent of his qualifying earnings during his "best 20 years", revalued in line with subsequent earnings growth to the date of retirement. The pension payment is index-linked to (at least) prices; if the pensioner dies, the surviving spouse inherits the whole of his or her pension.

6. On the other hand, a contracted-out SERPS member on retirement receives his GMP as part of his occupational pension. The value of the GMP at award is somewhat lower than the equivalent contracted-in pension because it is based on (revalued) average earnings over the member's whole working life, not on the "best 20 years". The inheritance provisions for GMPs are also less generous. In line with general occupational scheme practice, the surviving spouse only inherits one half of the pension.

7. The contracted-out SERPS member's earnings-related pension payment from the State is equal to the difference between the full index-linked contracted-in pension and his GMP which is constant in money terms. The State therefore makes up the difference between the "best 20 years" and "career average" pension awards, and guarantees inheritance of the full GMP by the surviving spouse. These provisions account for about one-quarter to one-third of projected future state earnings-related pension payments (called the "additional component", AC) to contracted-out SERPS members and

their surviving spouses. The remaining 60-75 per cent of state payments of AC to the contracted-out is the cost of index-linking the GMPs in payment (ie post award). Total payments of AC to contracted-out SERPS members is estimated to amount to about 45 per cent of the total estimated pension cost of SERPS in 2033-34.

8. Table 1 shows the distribution of present and future pension payments (including lump sums) under both the National Insurance Scheme (flat-rate pension plus SERPS) and Occupational Schemes. The figures are also shown as a percentage of total wages and salaries. The GMPs provided as part of occupational pensions in payment in 2033-34 are shown in brackets, below the figures (in row 2(ii)) for the cost to the SERPS of making these up to the fully index linked pensions available to those contracted in.

2. The Future "Burden" of SERPS

9. Since pensioners are non-producers, command over the resources they consume has to be transferred from producers by means of taxation or a share in investment income. The future claim on resources by pensioners relative to that of non-pensioners (ie the future "burden" of pensions) can be proxied by relative prospective income flows, which represent claims over resources. Various measures of these flows have been used in the recent debate and one example, total pension payments relative to total wages and salaries, is shown in Table 1. This shows the ratio of pensioners' income to total wages and salaries growing from 14 per cent in 1984-85 to about 22 per cent after 40 years, if basic pension is price uprated, and to about 27 per cent if the basic state pension is earnings linked. If the overall pension share were only to rise in line with the ratio of pensioners to workers (ie the "demographic effect") the ratio after 40 years would be 18 per cent. This helps to put the projected actual rise in the pension share into perspective.

10. Pension payments relative to total wages and salaries, are rather unsatisfactory as a measure of "burden" as they do not represent the final relative income position of the two groups. Taxation, claims to means-tested benefits and other income transfers between the two groups are ignored. Perhaps a better measure of pensioners' final claims on resources (relative to non-pensioners) is given by the DHSS economists' projections of pensioners' share of total disposable income (TPDI). This takes account of tax and NI contributions, and SB and HB entitlements and the like. (For

this reason they are subject to a very high degree of uncertainty.) The figures are shown in Table 2.

11. The future "burden" of financing State National Insurance Scheme pensions on a PAYG basis which would fall directly on employers and employees next century can alternatively be represented by notional NI contribution rates. Table 3 shows separately the "demographic effect" on future contribution rates for financing SERPS and basic pension respectively. (It should be noted that the notional contribution rates cover the cost of the contracted-out rebate). It also shows the ratio of the different components of State pension expenditure as a percentage of GDP, with and without the "demographic effect". In both cases the future "burden" is reduced once the "demographic effect" is removed. This allows one to distinguish the effect of demography from the effect on costs of maturity of SERPS benefits, the method of indexing basic pension and so on.

TABLE 1 PROJECTED PENSION PAYMENTS, 1984-85 TO 2023-4

(£ billion, 1984-85 prices)

	1984-85 £b	% of total wages and salaries	2023-4 £b	% of total wages and salaries
National Insurance Scheme				
(1) Flat rate pension (including graduated benefits)	15	9½		
(a) Price-uprated			20	7
(b) Earnings-uprated			34	12
(2) Earnings-related pension (SERPS) of which	v. small	-	16	5¾
(i) Contracted-in			9	3¼
(ii) Contracted-out			7	2½
(GMPs)	v. small		(5)	(2)
Total NIS pension expenditure	15	9½	36-50	12¾-17¾
Occupational Schemes	7½	4½	25-27 (1)	9-9½
of which				
(a) Unfunded public sector (2)	2½	1½	9-10	3¼-3½
(b) Funded public and private sector	5	3	16-17	5¾-6
Total Pensions				
(a) With basic State pension price-related	22½ (3)	14	61-63 (1)(3)	21¾-22¼
(b) Basic Earnings-related			75-77 (1)(3)	26¾-27¼

NB: These figures are heavily rounded.

(1) A range of figures is given for occupational schemes to cover the possible improvement in future benefits, in particular early leavers' protection and extension of price-linking.

(2) This includes most public service schemes (for local government includes only unfunded pension increase payments). The projections are very uncertain.

(3) Total unfunded pension expenditure (NIS plus unfunded public sector) rises from £17½ billion in 1984-85 to £45-60 billion in 2023-4, but its share of total pension expenditure remains constant at about ¾.

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Sir PM

SECRET until 3 June 1985

FROM: MS D J SEAMMEN

DATE: 31 May 1985

CHANCELLOR OF THE EXCHEQUER

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Sir P Middleton
Mr Bailey
Sir T Burns
Mr Anson
Mr Byatt
Mr Kemp
Mr Battishill
Mr Monger
Mr Watson
Mr Culpin
Miss Noble
Mr Cropper

FQ

PES:PP.

SOCIAL SECURITY GREEN PAPER: BRIEFING

The Green Paper is to be published on Monday. Mr Fowler will be circulating tonight summaries for the press, factual briefing notes and defensive Q and A briefing. I understand all this is to go to No 10 tonight, and will be copied to us. We will circulate it widely on Monday.

2. I have discussed with Sir Peter Middleton and Mr Culpin the general line to take for the Treasury Press Office and for Treasury Ministers' use, eg in Finance Bill debates. We recommend that while the general line should of course be supportive of Mr Fowler's proposals, we should confine direct comments to matters of specific Treasury interest. These include

(i) the effects of the proposals on public expenditure and the PSBR;

(ii) the effects of the pension proposals on public service pensions;*

(iii) tax aspects of the pension proposals;

* To follow from S Division on Monday

(iv) macro-economic effects of the pension proposals;

(v) interaction of the proposals with your own Green Paper on Personal Taxation, and generaly the interface between tax and social security;

(vi) (for possible use in Finance Bill) the proposals on mortgage interest.

3. There is in fact rather little to say on many of these topics given the general lack of quantification in the Green Paper. I attach a brief line to take on these issues, together with, where available, relevant pieces of the draft DHSS briefing.

DS

MS D J SEAMMEN

PS. We have been assuming that, as before, the uprating of public service pensions should follow the social security uprating ie there will be a July 1986 uprating & April thereafter. Anything else could hardly be justified; the legislation links public service pensions to the soc. sec. uprating. There will be some (small) savings.
Do you agree please? DS.

GENERAL THEME OF GREEN PAPER

Case for reform self-evident. Existing system has helped to raise the living standards of the poorest and most vulnerable groups in society and provided a safety net against urgent need. But piecemeal development has resulted in multitude of benefits with overlapping purposes and differing entitlement conditions. The present complexity in benefit rules means the system is difficult to administer, at times impossible for public to understand; and help does not always go where help is most needed. The emerging cost of the state earnings related pension scheme is a problem which must be faced. Liabilities are building up rapidly: if action is to be taken, it must be now.

The Green Paper proposals are aimed at tackling these problems. They offer a clearer and simpler structure; one which is relevant to the needs of today and capable of meeting the demands into the next century. They reflect the fundamental principle that the system of social security provision should be based on a clear understanding of the relative roles and responsibilities of the individual and the State. Social security is not a function of the state alone. Most people not only can, but wish to make sensible provision for themselves. The organisation of social security should encourage that. It should respect the ability of the individual to make his own choices and to take responsibility for his own life, but recognise the responsibility of government to establish an underlying basis of provision on which individuals can build and on which they can rely at times of need. The State has an important role in supporting and sustaining the individual; but it should not discourage self-reliance or stand in the way of individual provision and responsibility. Green Paper proposals based firmly on this "twin pillar" approach.

General Line to Take

The Green Paper is a substantial and extremely important document presenting far reaching proposals. Culmination of 18 months work by review teams and careful consideration of extensive evidence submitted during consultation process (4,500 pieces of written evidence, 19 public sessions, in which 62 organisations and individuals gave oral evidence. Most fundamental examination of social security system since Second World War. Secretary of State to be warmly congratulated. Proposals based on clear concept of respective roles of state and individual: Government has responsibility to establish the underlying basis of provision on which individuals can build and on which they can rely on at times of need; but most individuals can and wish to make sensible provision for themselves, and the system should recognise and encourage that. Wholeheartedly endorse these principles. Detail of the proposals for further consultations before final decisions taken. Hope that Opposition and pressure grups are prepared to give proposals the careful consideration they warrant. They owe it to those affected by the proposals to participate in consultation process in constructive way. Leave it to My Rt Hon Friend to deal with substance of the proposals, as he is in far the best position to respond.

Line to take on Specific "Treasury" Interests

1. Effect on public expenditure, PSBR.

Main impact will be to reduce the long term cost of SERPS, reduce expenditure on housing benefit in the short term significantly, and lead to economies in administration. But precise financial effects cannot be given until final decisions are taken in the new structure, and the benefit rates to be paid are settled. (No change in public expenditure planning total).

2. Effect on individuals.

Precise effect on individuals cannot be given until final decisions taken on the new structure, and the benefit rates to be paid are settled.

3. Effect on incentives (poverty and unemployment trap)

Key feature of proposals on out-of-work income support, family credit and housing benefit means it should be possible both to ensure that those in work are better off than if they were not working, and to eliminate the worst effects of the poverty trap (ie no marginal rates over 100%). [NB - but more people in the poverty trap]

4. Effect on Firms

Family credit to be paid through employers, so some additional work. But should prove even simpler to operate than existing, successful statutory sick pay scheme. And significant advantage to employers because full net remuneration perceived more clearly by employees. Pension proposals mean some additional costs for employers. Green Paper fully acknowledges that (Vol 1 para 7.18, Vol 2 para 1.66). Inevitable consequences of starting to build up additional funded pension provision while cost of pay-as-you-go system continues unchanged. Net effect on employers and employees should be small, but inevitably there will be variations between individuals. Three year transition to enable costs to be absorbed as easily as possible. Full impact not until end of decade.

5. Effect on Public Service Pensions

See separate brief being prepared by Superannuation Division.

Macro-economic Effects

Immediate effects marginal in term of macro-economic management: no change to public expenditure planning total transitional arrangements mean changes to national insurance and pension contributions not fully effective until end of dcade. Increased private provision means that total net private savings should grow; to the extent that this lowers interest rates, domestic investment will be encouraged. In addition overseas investment should increase.

Tax Relief on Pensions

Green Paper makes it clear that contributions made to occupational and personal pensions under the new arrangements will be subject to the same tax relief arrangements as for other pension contributions, (Vol 2 para 1.45). Chancellor made it clear in his Budget Speech that he had no plans to change existing tax relief arrangements. Green Paper quotes total volume of additional contributions to private pension schemes rising to £1¼ billion in 1989-90. Amount of tax relief will depend on how total is shared between employers and employees; precise tax position of particular firms involved; and on other income of individuals concerned.

Relationship with Personal Taxation Green Paper, and Interface between tax and social security

Proposals wholly consistent with proposals for single transferable allowances announced in Budget, on which Green Paper promised later this year. As Chancellor said in Budget Speech (and confirmed in speech to Equipment Leasing Association on 28 May) the Green Paper will also look at pros and cons of a closer integration of the tax and social security system. Two aspects to distinguish: integration of tax and National Insurance Contributions; and integration of tax and benefit systems. On first, present contributory system has considerable merit. Brings home to people fact that social security has to be paid for. On second, attractions of greater alignment obvious, but differences between the two systems go deeper than the direction in which the payments are made. Green Paper will go into all this seriously and in depth.

Mortgage Interest

Green Paper notes that arrangements for paying mortgage interest of those on supplementary benefit very generous. Government to discuss with building societies and other interested parties arrangements whereby less of the burden - particularly for people on benefit for a short time - falls on social security system.

FLAG 4

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SOCIAL SECURITY REVIEW BRIEFING
EFFECTS OF PROPOSALS

Why changes in entitlements are unavoidable

* Major review of social security must mean changes.
* Inevitably entitlements will change so some will get more, some less. No point setting up a review if no changes can be made.

Effect of changes

* More help for low-income families (family premium in income support scheme, family credit scheme for those in work
* Changed entitlements in housing benefit and supplementary benefit - steps will be taken to minimise the impact of the change on [illegible] existing beneficiaries
* Changes will coincide with uprating of benefits in April 1987
* Changes to pensions, widows' benefits, maternity allowance, and family income supplement, will not affect entitlements of any existing claimants
* Improved incentives - income support, housing benefit, family credit, based on broadly same assessment rules to produce a more coherent structure; improved earnings disregards in income support scheme; use of net earnings means account is taken of tax and marginal tax rates will be kept below 100%; unemployment trap eased for those in worst position - families with several children and/or older children.
* Simpler system - should help claimants to understand and receive their benefit entitlements

Defensive points

* Too soon to give detailed analysis of effect of changes on individuals:
  - final decisions on structure yet to be taken
  - final decisions on rates not taken till nearer the time;
  - details subject to consideration in light of views expressed during consultation;
  - important to concentrate on structure rather than argue about final adjustments to benefit levels that can only be decided at the time;
  - steps will be taken to protect the most vulnerable at the time of the change.
  - given the level of expenditure on social security, and the paramount need for structural reform, unrealistic to expect to make changes and protect all existing entitlements.
  - precise staffing effects will be assessed as detailed proposals are drawn up - need to have right number of staff for the job is fully appreciated - full consultation with staff and unions.

Green Paper Reference

Volume 1 - para. 13.2

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Social Security Review Briefing

Pledges and Manifesto Commitments

Likely line of attack

* Prime Ministerial commitment on SERPS (letter to Brynmor John, 20 May 1983: "Nor are there any plans to change the earnings-related component of the state pension.")

  Secretary of State's comments when Inquiry into Provision for Retirement set up ("My aim in setting up an inquiry is no to call into question the fundamental pension structure that was established in the 1970s with all-party agreement, and to which I was a party.")

* No manifesto statement on changes to welfare state.

Positive points

* Manifesto commitment on pensions has been honoured.

  "In the next Parliament we shall continue to protect retirement pensioners and other linked long-term benefits against rising prices."

  We have done just that. Pensions have increased by 84% since we came to office, while prices have risen by only 77% over the same period.

* Every Government has a duty to review. With public expenditure of over £40 billion on social security, and no major review for 40 years, the time was right for a fundamental examination. Such a fundamental review inevitably meant looking at all aspects of pensions and social security to see how resources could be used most effectively.

* Manifesto gave clear commitment to review public services where required (p.24).

  "We are determined that our public services should provide the best possible value both for the people they seek to help and for the taxpayer who pays the bill."

  That is precisely what the review of social security has been about.

Defensive points

* There was no intention to dismantle or reduce provision when the review was set up. The review looked at evidence - such as projections of future pension costs by the Government Actuary on latest assumptions. The Government's proposals for change have been developed in response to that evidence.

* No political consensus on SERPS - Alliance not in favour. So it was right to look at future arrangements and consider what changes are needed.

* One clear theme to emerge from almost all the evidence to the review was the consensus on the need for radical reform. The Government have responded to that by these proposals for reform. There is now a further opportunity for comment and debate on those proposals - we have no intention of avoiding public debate. But the need for change is clear.

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SOCIAL SECURITY REVIEW BRIEFING

TAX AND SOCIAL SECURITY

The case for reform

(means-tested

* increasing overlap between payment of tax and receipt of social security benefits

play down

* social security and tax systems both involved in collecting money, assessing entitlement on basis of personal information, etc

* computerisation of PAYE and of social security opens up possibilities for improved links between systems

Government proposals

* retain contributory principle and reject grand designs for integrated tax/social security systems as inconsistent with twin pillar strategy:

  - wholly means-tested scheme (IFS) not acceptable because of effect on incentives and self-help

  - universal social dividend scheme (Sir Brandon Rhys Williams) not acceptable because too much expenditure not directed to those in need

* further examination of scope for administrative improvements:

  - collection of contributions and PAYE
  - assessment, delivery and taxation of benefits
  - possibilities opened up by computerisation projects

Selling points

* specific proposals build on importance of links between tax and social security:

  - payment of family credit by employers to reduce 'churning'

implies 3 tier system depends

  - contribution changes to reduce 'cliff-edge' effect

* further ideas to be published in Green Paper on personal income tax later this year

Defensive points

* important differences between tax and social security. Social security usually weekly paid, paid direct to claimant, responds quickly if circumstances change (eg unemployment); tax assessed annually, collected through employers, and need not respond quickly to changes.

* single review of all tax and social security impractical. Right to review social security first - to decide upon the correct objectives. Now looking at ideas for administrative improvements.

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STATE EARNINGS-RELATED PENSION SCHEME (SERPS) AND NEW PENSIONS FRAMEWORK

Case for change

* Future SERPS costs unacceptably high - £23 billion by 2033/4. Earmarks too much public expenditure; and burden on future contributors, of whom there will be proportionately fewer to numbers of pensioners.

* Occupational pension coverage static since the mid-1960s. Universality and complexity of SERPS - particularly contracting out arrangements - partly to blame.

Proposals for change

* SERPS to be phased out for men under 50 and women under 45 in April 1987, with no more rights accruing after 1989. For men 50+ and women 45+ SERPS continues in full (including contracting out) until retirement.

* SERPS to be replaced by requirement, phased in over the same two years, for all employees (except those still in SERPS, 16 to 18 year olds earners) to have occupational or personal pension cover. The minimum contribution to this additional pension to be 4 per cent of earnings, with the employer meeting at least half.

* Personal pensions (with some minimum contribution) to be an option for any employee; andfor employers wainting to offer them instead of a scheme.

* Basic national insurance pension to remain unchanged at the heart of the state system.

* All rights accrued under SERPS to be honoured; those for men aged 40-49 and women 35-44 to be enhanced, to bring their ultimate totalpensions more in line with those of immediately older and younger age-groups.

* Maximum flexibility in settling pension age in the new framework, with equal treatment for men and women. No changes to state pension age, but ideas for more flexible retirement invited.

* Self-employed not covered by new requirement.

Selling points

half ?

* Will give almost everyone in work an occupational or personal pension - at present the workforce do not have one.

* Allows a wider variety of occupational and personal provision than before.

* Achieves more equal treatment between men and women.

* Increases amount of savings and investment in the economy - up to 1¼ billion a year

SECRET until publication - then unclassified

* Removes ultimate burden of SERPS while still possible to do so.

* Ensures protection of accrued rights and position of older workers unable to build up much additional pension before retirement.

Defensive points

* Extra employment costs kept to a minimum. (Less than 1 per cent of liable earnings for contracted-in employers and employees combined.) Stipulating minimum level of contribution to occupational or personal pension limits employers' commitments.

* Even if SERPS affordable ~~if earnings rise more than expected~~ on optimistic assumptions about economic growth, wrong to pre-empt so much public spending; much of SERPS spending would go on adding to good occupational pensions.

* Detailed Inquiry into pensions could not avoid looking at SERPS. 1975 Pensions Act "consensus" based on assumptions about the future that have since proved unrealistic with no projections of costs for a mature scheme.

* ~~Public sector schemes will meet minimum requirement. Further consideration of how to accommodate~~ those outside schemes (mainly part-timers) and personal pensions..

Existing contracted out schemes (including public sector) will qualify automatically. Further questions on public service pensions to Treasury.

Volume 1, 5.2-5.4; Chapter 7. Volume 2, Chapter 1

* Tax relief will apply for contributions [illegible] generally. Further [illegible] consideration to Treasury.

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SOCIAL SECURITY REVIEW BRIEFING
CONTRIBUTIONS

To be rewritten

The case for reform

* The ending of SERPS for all but the 40(45s) and over means the end of contracting out for everyone outside that age-group.

* High marginal contribution rates create disincentives for both employers and employees.

* NI contributions and PAYE income tax both involve collecting money from employers, and also information about individuals - adding to the administrative burdens on business.

* Computerisation and other administrative reforms open up possibilities for improved links between PAYE and social security.

Government proposals

* Retain the principle that entitlement to benefits should be related to contributions paid - people in work paying for the benefits of those who are not, and in turn establishing their own rights to benefits when they need them.

* Phasing out of contracted-out rebate in 1987/8 and 1988/9. On present assumptions Single rate of contribution - about 15.5 per cent - from 1989/90 for everyone except those still fully in SERPS, who will pay about 4 per cent more. (All rates joint employer and employee).

* Budget has already proposed adjustments in the structure of contributions, to give assistance to both employers and employees at low wage rates.

* Further examination of scope of administrative improvements:
  - collection of contributions and PAYE (Lord Young leading interdepartmental follow-up to "Burdens on business" scrutiny)
  - possibilities opened up by computerisation projects.

Selling points

* Proposals keep NI contributions separate and identifiable - which most people prefer to their assimilation into general taxation in order to fund "free allowances from the State"...

* ... but further ideas for better alignment of NICs and PAYE to be published in Green Paper on personal income tax later this year.

* Reduction in NI rates for contracted-in means overall impact of new pension requirement on employment costs kept to a minimum (½% a side).

Defensive points

* Impossible to secure total alignment of tax and NICs: eg
  - tax paid on income; NICs on earnings
  - prohibitive cost (£6½ billion) of turning Lower Earnings Limit into a threshold for contribution, like tax threshold.

* Phasing in of new arrangements staggers effect of higher NI, contributions for contracted-out, increasing pension schemes room for manoeuvre.

Green Paper references

7.48

SECRET

Sir Pm

- 3 JUN 1985

FROM: MRS R LOMAX

DATE: 3 June 1985

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Sir P Middleton o.r.
Mr Bailey
Sir T Burns
Mr Anson
Mr Byatt
Mr Kemp
Mr Monger
Mr Watson
Mr Culpin o.r.
Mr Monaghan
Miss Noble
Mr Pratt
Mr Cropper
Mr Lord
Mr H Davies

MS SEAMMEN

SOCIAL SECURITY GREEN PAPER: BRIEFING

The Chancellor has seen your minute of 31 May. He agrees that our general line should be supportive of Mr Fowler's proposals.

2. The Chancellor has commented that we are bound to be pressed hard for our estimate of the total savings. The answer has to be that the review proposals will secure worthwhile savings over the medium term, and substantial savings in the next century. Ultimately public expenditure and PSBR figures will have to be given for the whole exercise. But we have to move on this in tandem with DHSS. However, we should take this opportunity to make it clear that we never sought £4 billion savings - or anything remotely approaching that figure.

3. IDT should also say that we are happy with the SERPS proposals now that they have been amended to meet our obejctives (which concerned burdens on the self-employed, employers and employees more than the PSBR). It also needs to be made clear - delicately - that we supported SERPS abolition, but had doubts about compulsion.

4. The Chancellor is content with your assumption about the uprating of public service pensions (your manuscript postscript).

5. The briefing on tax relief on pensions refers to the Chancellor's remarks in his budget speech; the Chancellor would prefer a formulation which sticks more closely to what he actually said.

RL

RACHEL LOMAX

SECRET

CHANCELLOR

FROM: D M WILLIAMS

DATE: 3 JUNE 1985

cc: Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Sir P Middleton
Mr Bailey
Sir T Burns
Mr Anson
Mr Byatt
Mr Kemp
Mr Battishill
Mr Monger
Mr Watson
Mr Culpin
Ms Seammen
Miss Noble
Mr Brook
Mr Cropper

SOCIAL SECURITY REVIEW: PUBLIC SERVICE PENSIONS

I attach the briefing on public service pensions referred to in Ms Seammen's submission of 31 May. It has been prepared mainly for use by the departments with responsibility for public service pension schemes and we intend to circulate it to them tomorrow along with copies of Chapter 1 of Volume 2 of the Green Paper. The text has been agreed with the DHSS and with ST Division.

2. You will notice the briefing does not include anything about uprating to which Ms Seammen referred in the post-script to her submission. I understand you have signified agreement with the recommendation in that post script. If, therefore, Mr Fowler includes the change in uprating pattern in his announcement today, we will add a question and answer to that effect before circulating the briefing to departments.

3. On a separate point (referred to in paragraph 8 of Mr Kemp's minute of 28 May), you will have seen from his letter of 29 May that Mr Heseltine has now agreed that the armed forces should not be exempted from the personal pensions arrangements on the understanding that that does not mean moving towards a directly

contributory scheme. We therefore saw no difficulty about including in the attached briefing an answer which says that public servants <u>will</u> be able to opt for personal pensions (Q6.).

Mike Williams

D M Williams
Superannuation
Division

IMPLICATIONS OF THE SOCIAL SECURITY GREEN PAPER FOR PUBLIC SERVICE PENSION SCHEMES

General

Q1 Do the proposals in the Green Paper apply to the public service pension schemes and their members?

A Yes. The government has no intention of exempting the public services from any of its requirements. Public employers and the public service pension schemes will be required to comply with all the requirements which would apply to other employers and schemes. Though the Government intends that the new occupational and personal pension arrangements that are to replace SERPS will be based on schemes which offer pensions in return for defined contributions, salary-related defined benefit schemes will also be able to qualify. The present contracted-out final salary pension schemes inthe public services are expected to qualify automatically.

Q2 If the country cannot afford unfunded, index-linked SERPS, how can it afford unfunded index-linked public service pension schemes?

A. The government has some control over the numbers of and the costs of pay and pension contributions of public service employees that in a way that it does not have in relation to the population as a whole. It can therefore take account of the cost of future public service pension liabilities in determining how many public servants there should be, what pay increases can be afforded for them and what their pension contributions should be. (There are particular difficulties with pay, see the answer to Question 17)

Indexation

Q3 Does the Green Paper have any implications for the indexing of public service pensions?

A. Not directly, comments are invited in the Green Paper on how far schemes should be required to provide inflation-proofing after retirement.

Q4 What about the government's manifesto commitment on indexation of public sector pensions?

A. The government stands by its commitment to continue to protect public sector pensioners against the effect of rising prices on the basis of realistic contributions. It believes that the way to contain the cost of index-linking and to narrow any gap that exists between the increases received by those with index-linked pensions and those without is to bring inflation down and to keep it down.

Q5 What then is the government doing about ensuring that there is a basis of realistic contributions?

A The contributions of some groups of pubic servants (policemen, firemen, MP's and MEP's) have been increased to what the government considers a realistic level. Some work has been done on the remaining public service groups but it was impossible to complete this work while the social security review was in progress. Further work will be done in the light of the Green Paper and response to it.

Personal Pensions

Q6 Will public servants be able to opt for personal pensions?

A Yes. It would be unreasonable to deny public sector employees the freedom afforded to other employees.

Q7 What will be the statutory requirements for personal pension schemes?

A. For the most part the requirements will be the same as those applying to occupational schemes which receive the minimum pension contributions. The minimum contribution proposed is 4% of earnings of which the employer will be required to meet at least 2%.

Q8 Will the employer be obliged to offer his employees the choice between an occupational scheme and the payment of contributions to a personal pension scheme?

A. There will be no obligation upon an employer to run an occupational scheme but where he does he will be obliged to allow his employees to opt out of it and have their minimum pension contributions paid into a personal pension.

Q9 Will personal pension schemes be required to cover benefits other than provision for retirement?

A. Personal pension schemes to which minimum contributions are paid will be required to provide retirement and contingent benefits for widows and widowers but not for redundancy or injury benefit. It is expected that these latter will continue to be a liability to the employer.

Q10 Does that mean that the employer will be able to exclude any of his employees who opt for a personal pension from any ancillary arrangements he has for redundancy/early retirement and injury benefit?

A. The Government will want to consider wider implications of the proposals in the light of responses to the Green Paper. Employers should not penalise people who opt for a personal pension.

Q11 Since the benefits of these ancillary redundancy and injury benefit schemes are based on rights accrued under the main pension scheme, how can they be applied to people who opt out of the main scheme?

A. It will be for employers and their pension schemes to work out appropriate ways of providing the same level of benefit as would have been provided if the employees had remained within the scheme.

Q12 Will the employer be required to satisfy himself of the bona fides of a personal pension scheme before paying contributions to it?

A. The intention is that providers will give employers an appropriate certificate. All such arrangements will be subject to spot checks by DHSS.

Q13 Will employees be able to have accrued rights transferred into their personal pension schemes?

A Yes if they change jobs. If not the right to transfer accrued benefits will not apply to those earned before the implementation date of the new arrangements. Further consideration to transfer rights will be given in the light of the responses to the Green Paper.

Q14 Will employers/occupational schemes be obliged to accept applications from personal pensions optants to re-enter their schemes

A. This is for decision in the light of responses to the Green Paper but employers will be required to provide pension cover at at least the minimum level for all qualifying employees.

<u>Part-timers</u>

Q15 Does the Green paper mean that occupational pension schemes will have to admit <u>all</u> employees irrespective of the number of hours a week they work?

A. No. But it does mean that employers will be liable for an employers contribution either to an occupational or to a personal pension scheme, on all employees who earn more than a certain amount per week, probably the lower earnings limit for national insurance contributions.

Q16 How will the cut off be interpreted in the case of workers with variable earning patterns?

A. Probably with some kind of averaging, but this is for discussion in the light of responses to the Green Paper.

Financial arrangements

Q17 Will non-contributory occupational schemes have to go contributory?

A. Not necessarily. Since, however, in contributory schemes employers will be unable to continue to deduct employees' scheme contributions from those who opt for a personal pension, former members of non-contributory schemes may feel they are entitled to an increase in pay in exchange for opting for personal pensions. In general the arrangements for personal pensions will sit more comfortably along side contributory schemes than non-contributory ones.

Q18 Does the Green Paper have any implications for the funding arrangements of occupational schemes?

A. Not as such. There may, however, be increased pressure from some staff interests in public service schemes for widening of the notional investment portfolio for notionally funded schemes.

17

CONFIDENTIAL

FX PES:P.P.

From: D R H BOARD

Date: 4 June 1985

MR ODLING-SMEE

cc Sir T Burns
Mr Byatt
Mr Mowl
Mr Riley
Ms Seammen
Mrs Holmans
Mr Hood
Mr Pratt
Mr P Spencer
Mr Short

ECONOMIC EFFECTS OF COMPULSORY PRIVATE PROVISION OF PENSIONS

Sir Peter Middleton was grateful for your minute of 31 May and looks forward to the finalised report and your answers to the questions raised in Sir Peter's minute of 15 April*. Having read the section in the draft report which begins with paragraph 23, Sir Peter is still not clear why the overall level of savings and investment in the economy should be higher with a fully funded scheme. If nominal incomes are held constant and markets operate perfectly, Sir Peter does not see why there should be this effect. Does this not mean the transitional fall in output has to be fully offset? And why should a tendency for saving to increase be a reason for reducing the growth of money GDP?

Douglas Board

D R H BOARD
Private Secretary

(*attached)

FROM: MRS R LOMAX
DATE: 3 June 1985

cc Chief Secretary
Financial Secretary
Minister of State
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Bailey
Mr Anson
Mr Scholar
Mr Watson
Ms Seammen
Mr D Williams
Mr Gilhooly
Miss Noble
Mr Cropper
Mr Lord

MR KEMP

SOCIAL SECURITY REVIEWS - PUBLIC SERVICE PENSIONS

The Chancellor has seen your minute of 28 May and Mr Heseltine's minute to Mr Fowler of 29 May.

2. The Chancellor thinks we can go along with Mr Fowler on the same terms as Mr Heseltine, given no backdating.

RL.

MRS R LOMAX

SECRET

From: SIR PETER MIDDLETON

Date: 15 April 1985

MR ODLING-SMEE

cc Sir T Burns
Mr Byatt
Mr Anson
Mr Riley
Ms Seammen
Mr P Spencer
Mrs Holmans

ECONOMIC EFFECTS OF COMPULSORY PRIVATE PROVISION OF PENSIONS

I have taken a glance at Mrs Holmans' piece attached to her minute to you of 12 February. Obviously this is very much a first shot. But I hope that we could move on quickly to try and put some numbers on the possible effects, and also to consider the implications for fiscal and monetary policy. I should certainly like to be clear about these when the Green Paper is published.

2. On the substance I am not at all clear why, if markets are working properly, there should be any effect on the level of net savings in the economy. And even if markets are imperfect it seems to me the only problem one has is one of timing. The main question in my view concerns the quality of the investment produced by the savings. If the investment is done by a pensions institution rather than the public sector or individuals, will GNP in the long run be increased?

3. Of course one cannot avoid relying on future generations for the pension of any particular set of future pensioners. Future generations have the votes which determine fiscal policy which itself has a decisive effect on savings in the economy as a whole. And as we know these generations might even want to tax pension funds.

P E M

P E MIDDLETON

021-663

PSP

CONFIDENTIAL

FROM: R J DEVEREUX
DATE: 4 June 1985

1. MISS PEIRSON MEP
2. CHANCELLOR OF THE EXCHEQUER

cc Sir P Middleton
Sir T Burns
Mr Cassell
Mr H P Evans
Mr Battishill
Mr Lankester
Mr Watts
Dr I Webb

CGBR IN MAY

The preliminary estimate of the CGBR in May is £1.4 billion, bringing the cumulative total since 1 April 1985 to £2.3 billion. Within this the CGBR(O) is estimated to have been £1.3 billion in May and £2.4 billion since 1 April 1985. These figures are not yet firm and may change with later information before publication on 18 June in the monthly press notice on the PSBR.

2. The CGBR(O) outturn for May is £0.2 billion lower than the forecast made a month ago. The main factors are higher Customs and Excise receipts (by £0.2 billion) and a larger surplus on the National Insurance Fund (by £0.2 billion) partly offset by lower Inland Revenue receipts (by £0.1 billion) and other changes.

3. The cumulative CGBR(O) since 1 April 1985 is £0.9 billion lower than forecast in the Budget profile. Higher Customs and Excise receipts account for £0.5 billion, the larger surplus on the National Insurance Fund accounts for a further £0.2 billion, and supply expenditure is slightly lower than forecast. Inland Revenue receipts are consistent with the Budget profile.

4. Further analysis of the outturn in May, and the implications for the next three months, will be given in the next Ministerial note on the PSBR in two weeks' time.

R J DEVEREUX

CENTRAL GOVERNMENT TRANSACTIONS (2)

£ billion

	Inland Revenue	Customs & Excise	Other own account	CGBR(O)	Net Lending LAs	Net Lending PCs	CGBR
1st April 1985 - 31 May 1985							
Outturn (1)	+7.3	+6.4	-16.2	-2.4	-0.1	+0.3	-2.3
Budget profile	+7.3	+5.9	-16.6	-3.4	-0.4	-	-3.8
Difference	-	+0.5	+ 0.5	+0.9	+0.3	+0.3	+1.5
1st April 1984 - 31 May 1984	+6.7	+5.3	-15.2	-3.2	-0.5	+0.2	-3.5
Calendar May 1985							
Outturn (1)	+3.6	+3.1	-7.9	-1.3	-0.1	-	-1.4
Last month's forecast	+3.7	+2.9	-7.9	-1.4	-0.2	-0.1	-1.7
Difference	-0.1	+0.2	-	+0.2	+0.1	+0.1	+0.3

(1) Preliminary estimate, subject to revision

(2) + indicates a receipt, net receipt, or difference which reduces the CGBR

- indicates a payment, net payment, or difference which increases the CGBR