CABINET

NATIONAL INSURANCE BENEFITS

MEMORANDUM BY THE MINISTER OF PENSIONS AND NATIONAL INSURANCE

Introductory

In The Queen's Speech at the opening of the Session we have said that we are going to keep the position of those who are receiving national insurance benefits (and war pensions) under close review; and it is, I think, now accepted that an increase in the rates of those benefits and pensions will have to be made during the Session. The purpose of this paper is to canvass, as far as can be done at present, the major problems which will arise in connexion with such an increase, and to seek the Cabinet's agreement to the solutions I propose to those problems.

Amount of the increase and timing and scope of the Bill

2. It is not yet possible to come to a conclusion on the actual amount of the increase that needs to be made. That will have to be decided nearer the time of the introduction of the Bill and will depend upon the movement of the relevant earnings, prices and other indices up to that time and the state of the national economy. I should, however, tell the Cabinet now that I cannot conceive that we could make an increase of less than 7s. 6d. in the single uniform rate of benefit under the national insurance scheme, with corresponding increases in the other rates and increases also in the benefits under the industrial injuries and war pensions schemes which would broadly maintain the relationships between those three schemes as they exist at present. We made the basic single rate of benefit 32s. 6d. in 1952, increased it by 7s. 6d. to 40s. 0d. in 1955, by 10s. 0d. to 50s. 0d. in 1958, and by 7s. 6d. to its present level of 57s. 6d. in 1961. Any increase of a lesser amount would I think clearly be politically quite unacceptable. I give in paragraphs 4 to 10 below my reasons for the view that the increase to be made should take the form of a straightforward increase in the basic rates rather than of differential increases for different classes of beneficiaries.

3. On timing it is again, I think, too early at the present time to arrive at any decision about the date of the introduction of the Bill, which will be dictated by the general requirements of the Parliamentary time-table. Early spring may well be a convenient moment, with a view to the increases coming into operation in the autumn; but if the Cabinet agree, as soon as we have reached decisions on the issues which I am submitting in this paper instructions can be given to Parliamentary Counsel to prepare a skeleton Bill. The Bill could thus be ready for introduction at short notice at any time from the end of January onwards. I should however warn the Cabinet at this stage that the complicated nature of the graduated pensions and contracting out provisions involved will make the Bill somewhat longer than past increase Bills and offer much scope for Parliamentary debate.
Differential benefits

4. The first major issue is whether the increases in national insurance benefits should be made in the same way as in 1955, 1958 and 1961—that is to say, by uniform increases for all beneficiaries—or whether there should be any form of differential increases favouring any special class or classes.

5. At the 1959 election—prior to the last benefit increase—we undertook to ensure that pensioners continue to share in the good things which a steadily expanding economy will bring. In the debate which took place on an Opposition Motion last March, the Government’s Amendment expressed confidence that we should continue to ensure that recipients of national insurance and other social security benefits “share in the rising standards of the nation” but did not single out pensioners in particular. From what was said in the debate, however, and from such soundings as I have made it is clear that many of our supporters feel that “the old” have a special claim to consideration, particularly because of the erosion of their savings through inflation. This feeling is often linked with the view that we should try to ensure that increased benefits are given on a selective basis where they can be of most help to the individual—with a strong tendency to view the older retirement pensioners as a needy class and to place them highest on the list of priorities. I have therefore been considering whether, as part of the next increase in benefits, something extra could be done for the aged.

6. One way would be to pay a higher rate of pension for both sexes from 70, the age when pension is payable to men who satisfy the contribution conditions whether or not they have ceased working. Seventy is also the age at which war widows receive an additional 10s. Od. a week. The exact amount of any increase, whether with a differential for the old or not, is as I have said a matter of judgment to be decided at the appropriate time. But it may help to clarify the general issues of principle if I put into money terms the sort of differential scheme that would be possible by taking the cost of a uniform increase of 7s. 6d. for a single person, which as explained in paragraph 2 is the minimum uniform increase which in my judgment would be acceptable. Within about the same level of cost, it would be possible instead to raise by 5s. Od. the single rate of retirement pension for those under 70 and of sickness, unemployment and other national insurance benefits, while retirement pensioners over 70 could be given an increase of 10s. Od., thus creating a 5s. Od. “differential” for them.

7. This course has the attraction that it offers a way of meeting the desire of some of our supporters for greater selectivity in the distribution of benefits. But it is to my mind open to several objections both in the national insurance and in the national assistance fields. To take national insurance first:

(i) The amount of the differential could not be large. A differential of 5s. Od.—that is, the difference in my example between a preferential rate of 67s. 6d. for single pensioners over 70 and a rate of 62s. 6d. for younger pensioners and for other national insurance beneficiaries—might be criticised as insignificant. The differential could be increased within the same total cost only by further reducing the size of the increase for the younger pensioners and other beneficiaries. For example, if the latter were increased by only 4s. Od., it might be possible to increase the over-70 rate by 12s. Od.

(ii) Admittedly, we could show that the total cost of a differential scheme as in paragraph 6 was equal to the cost of a uniform increase of 7s. 6d. But it seems to me questionable whether, even with a differential scheme, an increase of 5s. Od. for the group not receiving the differential—that is, the younger pensioners and other beneficiaries—would generally be regarded as adequate, bearing in mind our past increases and pledges for the future.

(iii) It is often said that there is a strong political appeal in the proposition that retirement pensioners over the age of 70 form a class whose circumstances on the average warrant special state insurance provision. But it could not be said that most of those who would receive the differential were those in the greatest need; and a differential would not satisfy the school of thought among our
supporters which considers that improvements in benefits should be
more selectively given on the basis of individual need. It certainly
would not please the under-70 retirement pensioners with few
resources apart from their pension.

(iv) Doubts as to the justification for such a differential would make it the
more difficult in the long run to limit it to the over-70's. There would
be a sense of grievance among pensioners compelled by their
circumstances to retire earlier, for example, because of chronic ill
health, redundancy or the retirement rule in their calling. They
would compare their position with that of the pensioners receiving the
differential who had been able to work up to 70 and so had earned a
larger pension—at present up to about £1 more, with further additions
if they had contributed under the graduated scheme—and who might
even still be at work over that age. In 1951 the Labour Government
intended originally to confine their scheme of increases in retirement
pensions to those aged 70 or over (65 for women) but were forced by
their own backbenchers to extend this differential arrangement to all
who had reached minimum pension age on the appointed day. The
following year we removed the differential and took credit for
restoring uniformity of benefit rates. Moreover, a differential increase
for retirement pensioners over 70 would provoke demands for similar
treatment for younger groups who attract public sympathy, such as
the long-term sick—demands which could hardly be met without creating
grave anomalies.

8. The introduction of a national insurance differential for pensioners over
70 would raise complications for national assistance. Unless parallel increases
were made in national assistance, it would be said (however illogically) that as
regards pensioners over 70 receiving substantial national assistance supplementation
we were giving with the one hand and taking away with the other. That objection
could be forestalled either by introducing a preferential national assistance scale
for the over-70's or by disregarding for national assistance purposes the national
insurance differential. Each of these courses, however, has its own difficulties
and dangers:

(i) A national assistance differential for the over-70's, whether to match
a similar differential on national insurance or not, is out of keeping
with what has so far always been the basic conception of national
assistance. The twin foundations of national assistance are (a) the
scale rates (with rent allowance for householders) for what might be
called the national average needs of various categories (single
householder, married householder, lodger, etc.) and (b) the use of
discretionary allowances to supplement the means of the individual
whose particular circumstances whatever his age bring his needs above
the general level of his category. Within this structure, there does
not seem to be any place for treating the over-70's, whatever their
scale rate category, as if their needs were always greater than those
of under-70's in the same category; nor do I believe that a preferential
scale rate for the over-70's could long withstand the pressures on
behalf of younger people, for example invalids, whose needs and
hardship as individuals were fully as great. In so far as the needs of
individual old people are greater than those of others the National
Assistance Board can meet them by their discretionary payments, as
they are doing already for two-thirds of the pensioners on national
assistance.

(ii) The alternative of disregarding the national insurance pension differential
for the purpose of national assistance would not help the people over 70
without any national insurance pension who are receiving national
assistance—a group of nearly 200,000 in which are probably to be found
the most needy of all. Moreover, introducing a disregard of some part
of the national insurance retirement pension—which would involve
legislation—could hardly fail to provoke demands for the disregard to
be extended to other parts of the retirement pension. Indeed there has
already been pressure to disregard what is added to retirement pension
by way of increments for deferred retirement and of graduated pension. Such extensions of disregards, by increasing the proportion of pensioners receiving national assistance, would inevitably increase its cost. In turn demands would be stimulated for further increases in the standard rate of pension.

For these reasons, unless we are prepared to maintain that the needs of the over-70's differ in quality from all others and exceed them in magnitude in such a way that they cannot be met by discretionary allowances, neither course seems to me defensible.

Flat-rate increase

9. I conclude that, despite the attractions of a differential increase provided it were large enough, the balance of advantage lies in making the next changes in national insurance benefits and national assistance scales follow the conventional pattern of uniform increases. (This does not mean of course that we should not continue to give preferential national insurance treatment to the widowed mother through her children's allowances, and possibly, as regards her pension, by some relaxation of the earnings rule.)

10. There remains the underlying question of what is the desirable relationship between the national insurance increases and the improvements in the national assistance scale rates which would be needed at the same time. At present the national insurance rate for a single person happens to be the same as the national assistance scale rate (57s. 6d.) for a single household—but taking the rent allowance into account, as we must, the national assistance rates have a substantial lead. If an equal increase were made in both the national insurance and national assistance rates, that lead would be maintained. But in the past national assistance scales have moved more frequently than national insurance rates. For example assistance improvements were made in September 1959 and in September 1962 when there was no change in the national insurance provisions. So far it has been our policy to compensate for these “in-between” increases in national assistance by giving a smaller national assistance increase when national insurance rates are raised. My own view is that it would be sound and more in keeping with feeling in the country to maintain this pattern at any rate for the present. To depart from it by keeping the present relationship between national insurance and national assistance payments at the next move would restrict the Government's freedom of action in future; for when a subsequent move on national assistance was needed the Government would be faced with the dilemma either to allow national assistance rates increasingly to outstrip national insurance benefits or to make a premature national insurance increase. To go further and make a greater increase in national assistance payments on a differential basis for old people alone than in national insurance benefits would represent a swing towards reliance on means-tested rather than insurance benefits which would be highly controversial, and although it might be welcomed in some quarters it would be bitterly attacked in others. Moreover it might be unwise to make a move in this direction until we are able to review our social security arrangements with a better knowledge of what may be involved here by entry into the Common Market. This consideration seems to indicate that the next change in national insurance and national assistance should be a holding operation and not an uncharted move on what might turn out to be the wrong course.

Finance

11. Since at this stage I am not seeking the Cabinet's agreement to any particular figure for the increase in benefits, it would be premature to elaborate precise figures of cost, although it will illustrate the order of what is involved if I explain that a 7s. 6d. increase in the basic single rate of national insurance benefit would cost about £150 million in the first full year (and consequential increases in industrial injuries benefits and war pensions would cost an extra £19 million). There are, however, two questions of principle on meeting that cost which will need to be decided whatever the figures may be. The first is what increase, if any, should be made in the span of income liable to graduated contribution. The second (which is dependent on the first) is by what amounts contributions should be increased for those who are contracted out of the graduated part of the scheme.
12. The purpose of the graduated contribution was twofold—first, to enable the contributor to increase his pension in relation to his earnings and, second, to get from it a substantial and buoyant subsidy towards the growing cost of the flat-rate national insurance scheme and so keep down the contributions of lower-paid workers to a tolerable level. Since many employers had already made provision for their employees' retirement by way of pension schemes, and it was desired to encourage the spread of such provision, it was thought right to allow those employers who wished and whose pension schemes could satisfy certain conditions to contract out of the graduated scheme. It was thought originally that about 2½ million employees might be contracted out. So far about 4½ million have been contracted out. In order that those contracted out should not escape entirely from making any contribution towards the solvency of the national insurance scheme, they are obliged to pay a higher contribution than the flat-rate contribution paid by people in the graduated scheme.

Range of earnings attracting graduated contributions

13. Under the National Insurance Act, 1959, the range of earnings on which graduated contributions were payable was fixed at £9 to £15. Average industrial earnings have now substantially increased. In April 1962 they were £15 12s. 10d. a week for men—above the maximum for graduated contributions—as compared with £12 15s. 8d. a week in October 1958 when the £9–£15 range was first announced in the White Paper on Provision for Old Age (Cmnd. 538). It therefore seems not unreasonable to extend the range of graduated contributions—indeed, if this were not done the scheme would in the not very distant future become once again a mainly flat-rate one, at any rate for men, with everyone paying contributions on earnings of £15 a week. The last increase in benefits in April 1961 was financed by increases in flat-rate contributions because it was felt that it would not be feasible to alter the graduated scheme at the moment of its inception. It seems inevitable that on the occasion of the next increase some part of the cost should be financed from graduated contributions—indeed, I see no real alternative to increasing the range. What we shall have to decide is by how much. My provisional view is that, assuming the kind of increase in flat-rate benefits I have in mind, the range should be increased from £9–£15 to £9–£18. This would seem reasonable in relation to the movement of earnings. Such enlargement of the graduated scheme would, I think, be accepted as consistent with what we said in the White Paper (paragraphs 32 and 33) about the problem of dimensions of a State Scheme and the need to avoid excessive extension of compulsory State provision.

14. The increase in the range would produce an extra £44 million from graduated contributions in the first full year and this would enable the accompanying increase in flat-rate contributions to be kept within tolerable limits. For instance, the increase in the range would allow a 7s. 6d. uniform increase to be financed with an extra 9d. a side on the flat-rate contribution for employed men.

15. Any increase in the range is bound to cause some inconvenience to employers with contracted out schemes. The minimum amount of pension which these schemes are required to provide would have to be increased to match the increased graduated pension payable under the State scheme—from the present £2 6s. 2d. of pension per annum for each year of contracted out employment to £3 9s. 3d. It is estimated that, of a total of 21,000 pension schemes covering about 4½ million contracted out employees, about 8,000, covering rather more than 1½ million employees, would need to raise their minimum level of pension—which may in some cases relate only to the lowest paid workers in the scheme—to meet the new requirement. We shall have to allow a transitional period for necessary adjustments to be made, and it might be that some employers would wish to reconsider their position as regards contracting out. Most schemes however should have little or no difficulty in satisfying the new requirements for contracting out if the range of graduated contributions were extended to earnings of £9–£18.

16. I should warn the Cabinet that I doubt whether we could go on enlarging the scheme in the way and to the extent I have suggested every time benefits are increased in implementation of the Government's pledges. We shall need to give more thought to how the scheme is to develop in future; this may face us with complicated and difficult problems, and it is one of the points I have in mind in connexion with the review to which I refer in paragraphs 26 and 27 below.
Contracted out contribution

17. The relationship between the contracted out contribution and the flat-rate contribution paid by those in the graduated scheme was settled on grounds of convenience rather than of principle, the 1959 Act keeping the then existing level of contribution for the contracted out, while providing a reduced flat-rate contribution for those in the scheme. The relationship established in 1959 was preserved when benefits and contributions were increased in 1961. The contracted out contribution, though higher than the minimum contribution paid by the man earning £9 a week, is much lower than the contribution payable by the man in the graduated scheme who is earning around the present maximum of £15 a week and, even allowing for the fact that the man in the graduated scheme is earning graduated pension, the contracted out man at that level of earnings is paying less towards the cost of flat-rate benefits. As most of the contracted out are thought to be earning £15 a week or more, they are escaping their full share of the cost of flat-rate benefits. In this way private schemes have been encouraged to contract out but at some cost to the finances of the State scheme and to those paying graduated contributions in it.

18. If we increase the range of graduated contributions, we shall need to take account of this by raising the contracted out contribution by more than the increase in the minimum flat rate contribution paid by those in the graduated scheme. A substantial part of the extra graduated contributions will go towards meeting the cost of flat-rate pensions and the contracted out must also make a contribution to this. This is fair and logical and will not, I think, be unexpected by those familiar with the principles of the scheme. There may, however, be complaints from the lower paid among the contracted out that they will have to pay as much as they would if they were in the graduated scheme but without earning any State graduated pension. This may lead employers who have contracted out employees with earnings at the lower end of the scale to reconsider their position. While this is likely to be very much a minority problem in the private sector, employers in the public sector (including the Civil Service) may find it necessary to reconsider the present position where groups of their employees are contracted out irrespective of the level of their earnings. On the other hand a proportionate increase in the contracted out contribution will still leave most of the contracted out, who have relatively high earnings, in a favourable position compared with people with the same earnings in the graduated scheme. This throws into relief the disadvantage of a single flat-rate contracted out contribution, which will become more difficult to justify the wider the range of graduation becomes through successive increases.

19. One remedy would be to graduate contracted out contributions according to earnings as was suggested in 1958 by the Institute of Actuaries and the Faculty of Actuaries. Such a change, however, raises serious difficulties and would be impracticable on this occasion.

20. My conclusion is that we must keep a flat-rate contribution for the contracted out and that the amount by which it exceeds the minimum contribution payable by those in the graduated scheme must be increased at least proportionately to the increase in the range of graduated contributions; and that we should consider whether some small further increase might be desirable to avoid creating a vested interest in the present arbitrary relationship between the contracted out contribution and the flat-rate contribution payable by those in the graduated scheme.

Quinquennial increases of contributions

21. To keep receipts and outgoings in balance and, in particular to meet the steeply rising cost of flat-rate pensions over the next 15 to 20 years, the National Insurance Act, 1959, provides for quinquennial increases in the levels of all the contributions under the national insurance scheme. As from the beginning of the financial year 1965-66 (and at three subsequent five-yearly intervals thereafter) section 1(2) of the Act lays it down that fivepence a side shall be added to the minimum contributions, that the rates of graduated contributions shall be increased by one quarter per cent a side for employer and employee without ranking for extra graduated pension, and that ninepence a side shall be added to the contracted out contributions. Each of these quinquennial increases would yield about £80 million a year. It is, however, provided that the Minister can, by order made with the consent of the Treasury, vary these amounts to any lesser amounts which may be specified in the order.
22. The effect of these provisions, if left unamended, is that within a period which is likely to be not more than 18 months from the coming into operation of the new rates of contributions required in any case to finance the increases in benefits, there will be imposed upon contributors under the scheme a further contribution increase which will carry no increase in benefits with it. This seems to me to pose an awkward political problem.

23. I had considered whether to include a provision in the Bill to be taken this Session in effect advancing the date of the first quinquennial increases from 1965, by subsuming them with the other new and higher contribution rates provided in the Bill. The advantages would be that it would avoid two contribution changes within a space of perhaps 18 months; that the flat-rate contribution increases would be associated with benefit increases and, because of the increased income from graduated contributions, could be kept within tolerable limits; and that the increase in the graduated contribution would be allowed to rank for extra graduated pension.

24. On the other hand we would be strongly challenged for putting into effect contribution increases not currently needed to finance expenditure some 18 months before they were required and thus creating a substantial surplus in the first year.

25. I am therefore in favour of leaving the provisions in the 1959 Act for a quinquennial increase in 1965 unchanged and not increasing the level of contributions under the forthcoming Bill on account of it, although I am sure I shall have to make it plain when presenting my proposals to the House that, as the costings will show, the finance of the scheme will rely upon the quinquennial increases in contributions, the first of which will be due on 1st April, 1965, and will not earn any extra benefit.

Review of the scheme

26. I recognise that the outline proposals in this paper for a straightforward increase in national insurance benefits and a limited increase in the span of graduated contributions do not in any way constitute a "new look". In fact they would constitute a holding operation—that is a continuation of progress on our present course (which includes steady improvement in the real value of pensions) until we have a clearer view than we can have at present of the advantages and disadvantages of other paths which various schools of thought, both among our supporters and elsewhere, might have us take. My own view is that we ought not to venture along any of them without a comprehensive review of the whole field.

27. Apart from the need to present a forward looking public image in the social security field there are plenty of social security issues on which such a review would be valuable, provided the nature, composition and terms of reference of the reviewing body could be arranged so as to produce, as near as may be, responsible and objective recommendations. I refer to such issues as: the relationship between non-means tested benefits (national insurance and family allowances) and means tested benefits; the relationship between flat-rate and graduated contributions and benefits; the relationship to graduated contributions of the contracted out contribution; the question whether, and, if so, how, we should ultimately get the latter also on to a graduated basis but at a lower percentage; and, not least important, the apportionment among the various contributors to social security (employer, employee, tax revenue) of the amounts necessary to sustain whatever level and kinds of benefits the country can afford. Consideration of all these matters, particularly of the last, would have to take into account Common Market developments. It therefore seems to me that we would be wise ourselves to indicate our intention to institute a review. I would welcome the Cabinet’s views on this.

Summary

28. I ask the Cabinet to agree—

(i) that the next increase in national insurance benefits, to be undertaken sometime in the 1962–63 Session, should be a uniform one for all beneficiaries and include no differential elements (paragraphs 4 to 10);

(ii) that the span of earnings liable to graduated contributions should be increased (paragraphs 11 to 16);
(iii) that the amount by which the contracted out contribution exceeds the minimum contributions must be increased at least proportionately to the increase in the range of graduated contributions (paragraphs 17 to 20);
(iv) that no steps should be taken to advance the quinquennial increase in contributions due in 1965 (paragraphs 21 to 25);

and to consider—

(v) whether the announcement of the increase should be accompanied by an announcement that the Government were instituting an appropriate review of the basis and financial structure of the national insurance schemes (paragraphs 26 and 27).

N. M.

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