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E(80) 9

8th February 1980

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CABINET

MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

TAXATION OF BENEFITS PAID TO THE UNEMPLOYED
Note by the Chancellor of the Exchequer

1. At the meeting on 23rd January, E Committee asked that the date of introduction of the scheme should, if possible, be brought forward to the beginning of the financial year 1981-82: and that further consideration should be given to the staff numbers needed and the scope for offsetting savings.

A paper by Officials on these two points is attached.

2. So far as the first point - the date of introduction of the scheme - is concerned, the Inland Revenue could at a pinch make November 1981. While this is not at the commencement of the financial year 1981-82, it is an earlier tax year than originally proposed (1982-83) and it is close to the commencement of the 1981-82 wage round.

The other Departments, however, take the view that they cannot make a date earlier than April 1982; and their timetable, of course, determines the timetable for the project as a whole.

3. So far as staff numbers are concerned, we cannot realistically estimate a figure of less than 2000 for the three Departments combined. Obviously as the job progresses we would make every effort to cut this figure down. But as the Officials' Paper

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demonstrates in detail, 2000 represents a very, very big reduction in figures quoted not only before the Election but as late as the Summer of last year.

4. Of the 2000 staff required, 1400 would be Inland Revenue staff. This figure is as large as it is because of my agreement to accept the Method B ("subsequent") method of taxing benefits to meet objections raised by Colleagues. The effect of this has been to transfer a very significant part of the total burden in terms of staff needed from other Departments to the Inland Revenue. It would be intolerably unfair that my agreement to help colleagues in this way should now result in my being asked to absorb a heavy and disproportionate share of the total staff cost without any provision to meet it. As the Officials Paper discloses CSD themselves admit that provision has been made by Cabinet for growth and additional bids elsewhere, mainly in DHSS, DE and the Home Office. This ranks at least as high. I am not asking for extra staff: but what I must and do ask is that Colleagues should agree that if it proves necessary the staff cost for this project can legitimately be set off against the further savings of 5,400 listed in Annex 2 of the Lord President's paper (C(79)57). That after all is precisely the basis on which the figures were put forward, and agreed to be put forward, when the Lord President's exercise was undertaken.

Recommendations

5. The Inland Revenue, who would provide 1400 of the 2000 staff which, on the best estimates, would be needed to implement method B, could at a push make November 1981. However, the other departments involved - the Department of Health and Social Security and Department of Employment - say that they could not manage anything before April 1982. The paper by officials reflects this view.

I recommend the Committee:-

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- i) to invite the Secretaries of State for Health and Social Security and Employment to adopt a timetable which would bring unemployment benefits into tax from November 1981;
- and,
- ii) to agree that the staff cost for this project should, if necessary, be set against the further savings listed in Annex 2 of the Lord President's paper.

Notes for Introduction

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1. The Committee's view was that it was highly desirable that these benefits should be taxed, if possible, from 1981 rather than from 1982.

2. There are essentially G.H. issues in the preparation for taxing the benefits (though, naturally enough, they are closely connected). The first is to complete the job specification for the operation, covering such things as the procedures for maintaining PAYE compliance, the precise circumstances in which the benefits are to be taxed, and accounting and audit arrangements.

HM Treasury
8th February 1980

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NOTE BY OFFICIALS

TAXATION OF BENEFITS TO THE UNEMPLOYED

At the meeting on 23rd January the Chancellor was invited, in consultation with colleagues, to consider further the date for introducing the scheme to bring into tax benefits paid to the unemployed; and to consider the staff numbers which would be needed, and the scope for offsetting savings.

Date for Introduction

2. The Committee's view was that it was highly desirable that these benefits should be taxed, if possible, from 1981 rather than from 1982.

3. There are essentially two phases in the preparation for taxing the benefits (though, naturally enough, they are closely connected). The first is to complete the job specification for the operation, covering such things as the procedures for maintaining PAYE cumulation, the precise circumstances in which the benefits are to be taxed, and accounting and audit requirements.

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The second phase, on the basis of the job specification, is to design, programme and test the computer system required for the National Unemployment Benefit System's computers. The first phase involves the close co-operation of all the Departments involved in the precise definition of the functions of each one and the additional duties to be imposed on employers and claimants. We estimate that, if undertaken properly, it will require at least six months. The second phase, which is mainly for DHSS, is estimated to take a further 15 months. Assuming a final decision now, this takes us, in the best case, to mid-November 1981. Based on past experience of complicated exercises like this, our judgement is that a minimum of a further 3 months is needed to cope with any slippage or problems in the earlier stage, and to minimise the risk of a disruption in the payment of benefits when the new system goes live. This is not simply a matter of caution. Experience with past computer projects of this size and complexity, and indeed current ones, shows that a contingency period of this order is essential. Examples of this are the setting-up of the DVLC at Swansea and the introduction of the Police National Computer Unit; and, currently, the Civil Service Department's new computer installation at Chessington for pay and statistics has already used up a six months' contingency period. Some reasonable provision for slippage is an integral part of an exercise where deficiency or failure on the computer side would have severe operational and staffing consequences.

4. The view of the consultants, who made an independent and pretty hard-headed assessment of the project, was broadly similar. Their report said that an implementation date of November 1981 might be technically feasible, but they observed that this involved difficulties and risks and their recommendation was that the target date for implementation should be April 1982.

5. Ministers are, however, keen for an early start to the scheme. It is agreed that April 1981 is out of the question. As regards November 1981, we have to weigh the current presentational advantage of an announcement of a 1981 start with the difficulties we should undoubtedly be storing up for the future. Other

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departments believe that a November 1981 start would be too risky now to accept. The only way we could justifiably aim for it would be to more than halve the time required for the preparation of the job specification. The effect of this would be to exclude consideration of a number of important suggestions made by the consultants for staff-saving in the procedures. Even if this point is left aside, the job would be a rushed one and we should almost certainly find snags cropping up in the later phase of preparation which would cancel out any advantage gained. There are other considerations: the unemployment register is rising, which will put pressure on computer capacity; commencement in November 1981 will coincide with benefit uprating work; and introducing the scheme in mid-tax year is of itself more complicated than doing so at the beginning. Reluctantly, our view is that what is in truth little more than a presentational advantage is insufficient to outweigh the undoubted risks and probable extra staff cost of a November 1981 start.

Staffing

6. Officials have looked again at staffing numbers. We can confirm what the Chancellor said at the last meeting of E Committee: that with an April 1982 start date, and provided an announcement is made quickly, the estimate of 2,800 staff for a Method B scheme can be pared down to around 2,000.

7. The Chancellor was invited to reconsider this figure in the light of any revised estimate of the starting date. The figure of around 2,000 for April 1982 is already dependent on the successful adoption of various procedural changes leading to staff economies; there is no guarantee that that will happen. By the same token therefore it is inevitable that an earlier start date of even November 1981 would require more staff than that for April 1982.

8. So far as our public announcement is concerned, we suggest that it should make clear that the figure of around 2,000 is necessarily a preliminary estimate and that Ministers' aim will be to seek to lower it if this proves possible on more detailed examination of the procedures involved.

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9. Ministers may well judge that the Government's supporters will not have any cause to cavil at the figure. Bringing short-term benefits into tax has long been recognised as a complex and administratively daunting task. Under the last Government, as recently as last March, the figure of 10-11,000 staff was quoted for it (this included short-term sickness benefit, the large part of which we are proposing to tax separately at minimal staff cost). An official letter to the then Shadow Secretary of State for Social Services in the same month quoted up to 5,000 staff for taxing unemployment benefit. The report by officials last November put the staff cost in the range 2,940-4,050. Figures of this sort are still common currency: the Guardian at the end of last month gave 10,000 extra staff for a full scheme to tax short-term benefits and 3,000 for what they characterised as a "rough and ready" one. Taxing these benefits is a firm Manifesto commitment, which the Government would be fulfilling at considerably lower cost than is generally anticipated.

Offsetting Staff Savings

10. The revised estimate of 2,000 staff includes 600 staff in the Department of Employment and 1,400 Inland Revenue staff. The Department of Health and Social Security has agreed to absorb the staff cost there of some 90 posts.

11. As well as the savings from the administrative economies in 1979/80, totalling 1,600 staff, which will be carried through to later years, the Department of Employment Group is committed to savings of 12 per cent as part of the Lord President's exercise. These are on top of savings already achieved in the Unemployment Benefit Service through computerisation and fortnightly payment. The Department of Employment consider that the DE Group cannot in addition absorb the staff costs of taxing unemployment benefits without policy changes beyond those outlined in Annex 2 of the Lord President's paper (C(79)57).

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12. In the Inland Revenue administrative savings have already been made in order to perpetuate the 3 per cent cuts this year. Further administrative economies were included in the savings of over 5,500 staff promised by the Chancellor for the reductions in the Civil Service announced by the Lord President on 6th December 1979. Those firm savings were the most the Chancellor could guarantee to achieve by 1st April 1982 and left no contingency reserve or provision to take on new tasks such as this.

13. Further savings of the magnitude needed would therefore require further specific functional cuts. The wide ranging review last year identified all the options which could reasonably be contemplated. Further savings only by drawing on options listed in Annex 2 of the Lord President's final paper (C(79)57) and it would be unrealistic to think that there are other substantial options on which could be drawn upon to yield large enough savings within the requisite timetable. Indeed the Annex 2 options themselves are largely dependent on politically difficult decisions and on Budgetary changes which would reduce the tax yield. The Chancellor's ability to cut taxes in this way must be determined by the budgetary and economic context and he has had to withhold commitment to them for that reason. Though best efforts would be made to achieve these further savings, and so offset the cost of taxing benefits paid to the unemployed, this could not be guaranteed. The Department of Employment is in an even more difficult position in that changes to produce the required staff economies would go beyond those in Annex 2 of C(79)57.

14. The Civil Service Department have pointed out that the Government is committed to a programme of staff savings in the Civil Service of 12,400 posts in 1980/81 and 24,300 in 1981/82, increasing to nearly 40,000 posts a year in 1983/84 and beyond. Cabinet have already decided to provide for growth and additional bids, mainly in DHSS, DE and the Home Office, of 11,500 posts in 1980/81, and 12,600 posts in 1981/82 (rising to 18,000 if the latest unemployment assumptions are taken into account). These increases will broadly continue in the subsequent years unless there is a significant change in the underlying assumptions. The

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Government's programme will cease to be credible unless the staff costs of new proposals are from now fully absorbed by savings elsewhere.

15. The Government has, moreover, made clear that the savings announced on 6th December 1979 are only the first stage. There is a strong public expectation that further reductions will be made. The Civil Service Department are therefore reluctant that Annex 2 savings should be used to offset growth, instead of yielding further "real" savings. They accept that there may be occasions when it would not be practicable to offset the costs of new policies without drawing on the Annex 2 items. In the present case, however, their view is that with two years in which to plan it should be possible for Inland Revenue and the Department of Employment to identify economies which would suffice to offset their additional requirements.

Conclusion

16. Officials recommend that the start date for the scheme should be April 1982, and that the announced staff costs, put in the terms suggested at paragraph 8 above, should be around 2,000.

17. On the question of the offsetting savings, there is a difference of view. The Department of Employment and Inland Revenue would propose to use our best endeavours to achieve compensating savings, but failing this would have no alternative but to draw on those listed in Annex 2 of C(79)57. The Civil Service Department seek a firm agreement now that the requisite offsetting savings will be made, and that Annex 2 items should not be used. The Committee is invited to decide whether, and, if so, how the necessary resources should be provided.

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