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PRIME MINISTER

cc Sir Robert Armstrong

<sup>Flag A</sup> Family Support <sup>Flag C</sup>  
(MISC 111(85)6 and <sup>Flag B</sup> 11; the minute of 21 March from the  
Secretary of State for Social Services and  
MISC 111(85)1 Appendix 4)  
<sup>Flag D.</sup>

BACKGROUND

At present a flat rate child benefit of £6.85 a week is paid in cash to all parents in respect of each child <sup>under</sup> ~~over~~ 16, at a cost of £3950 million a year. Certain groups receive additional benefits costing £570 million a year. These are:

- One Parent Benefit - £4.25 a week, £100 million a year;
- Child Dependency Additions - £7.65 a week, £160 million a year;
- Child Special Allowance - £7.65 a week, £2 million a year;
- Family Income Supplement (FIS) - variable, £120 million a year;
- and,
- for those on supplementary benefit (SB) or FIS, free welfare milk and school meals - equal to £3.60 a week, £190 million a year.

2. All Governments since the war have accepted the principle of giving financial support to those who bear the extra responsibility of bringing up children. But so far the right balance has not been struck between families in and out of work; and between help through the tax or the social security system. There are too many different types of benefit, operating on dissimilar principles. Furthermore the real disposable income of families in the bottom income decile has fallen since 1979. Families with children on SB find it harder to manage than other recipients. For those in work, FIS does not adequately help larger families. Families in work can find themselves no better off, and even worse





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off, than those on SB and can pay marginal tax rates above 100 per cent. Benefits in kind are regarded as anomalous, contrary to freedom of choice and complicated to administer.

PROPOSALS

3. Against this background the Secretary of State for Social Services proposes:

- i. To retain universal flat-rate child benefit (at the present level, though the possibility would be kept open of restricting future upratings).
- ii. For unemployed families, to include a family premium element in SB (agreed at the last meeting).
- iii. For employed families on low incomes, to replace the child's special allowance and FIS with a system of family credits. Assessment would be as for SB, and payments made up of a flat amount plus additions per child. An illustrative scheme is at Annex 3 of MISC 111(85)6. The full benefit would go to those on net earnings of £36.10 a week, with a 50 per cent taper above that. Benefit would come through the pay packet, offset against tax and national insurance liability or, where necessary, taking the form of net additions to wages.
- iv. To replace benefits in kind (free milk and school meals) with cash additions of about £2 a week to family credit recipients and possibly to SB recipients at no net cost.

The net additional cost of the proposals is £67 million per annum. 500 staff would be needed. Probably 200,000 of the 350,000 eligible would take up family credits (FIS figures are 100,000 and 200,000 respectively). These families would gain on average £5 a week; larger families





with older children would gain £10 a week or more. A few smaller families would lose and require transitional protection.

4. In his memorandum MISC 111(85)11) the Chief Secretary does not comment on the Family Credit proposals but argues the case for finding savings of £1-1½ billion per annum from expenditure on child support. This is against the background of his wish to secure savings of about £2 billion per annum in total from social security, and the decisions at MISC 111's last meeting on housing benefit and supplementary benefit which will produce savings of about £3/4 billion per annum. He suggests that the options are:

- means-testing child benefit: a scheme limiting entitlement to incomes below £190 per week could produce net savings of £1½ billion. 3 million families would gain an average of £6.50 per week and 3½ million lose an average of £10.50 per week.
- cutting the level of benefit: eg. reducing the rate to £5.15 per week per child (from £6.85) would save £1 billion.
- restricting eligibility: eg to exclude the first child, or to include only the first and second child. Savings £1-1¼ billion.

The Secretary of State for Social Services argues (his minute of 21 March to you) against either means-testing or cutting the level of benefit substantially. Briefly he thinks the political cost too high. He does not comment on restricting eligibility. He suggests that some other options viz the introduction of a standard family tax allowance, offering the option of child benefit or a child tax allowance, and a modification of the independent taxation approach, might be explored and taken forward in the context of the Chancellor's proposed Green Paper on the reform of personal income tax.





## MAIN ISSUES

5. The main issues are:-
- (a) what quantum of savings should be sought from this area;
  - (b) how they might be found. Only significant changes to child benefit will produce substantial changes;
  - (c) whether FIS should be replaced by Family Credit as the way of supporting low income families;
  - (c) whether benefit in kind (milk and school meals) should be replaced by cash payments.

Savings

6. The arithmetic of the discussions so far suggests that savings of £1 billion or more per annum need to be secured from the child benefit/family support area if the Group are to get anywhere near the social security savings of towards £2 billion a year that the Chancellor and Chief Secretary are seeking. Present expenditure in this area is just over £4 billion which means savings of 25-30%. Clearly these can only be achieved by major changes of the kind proposed by the Chief Secretary, entailing substantial numbers of losers. If the Group shy away from such large savings in this area, but continue to have them as an objective for the review as a whole, they will almost inevitably have to look again at securing greater savings from housing benefit/supplementary benefit or at not uprating the unpledged benefits.

Changes to Child Benefit

7. Means-Testing The Children and Young Persons Review outlined a scheme (MISC 111(85)11 paragraph 5) which would remove child benefit from all families earning more than £190 per week (ie above average earnings). Savings could be up to £1½ billion, but the political and other costs might be very high. While 3 million families would gain an average of £6.50 per week, 3½ million would lose an





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← average of £10.50, an extra 2½ million families would be brought into means-testing, and the number of people facing marginal tax rates of over 75 per cent would be trebled.

8. Reduction in Value. To save £1 billion would require rates to be reduced to £5.15 per week (ie the 1981 level in cash terms). All recipients would lose.

9. Restricting Eligibility. The Chief Secretary suggests three possibilities - limiting eligibility to families with children under 12, restricting benefit to the second and subsequent children only, or (the opposite approach) to the first two children only. Each would save £1 - 1¼ billion.

10. Taxation. Mr Fowler suggests some possible changes to the tax system as an alternative (para 8 of his minute) for possible development in the Green Paper on personal tax. He does not quantify the possible savings and some of them might be small. Necessarily they will not take effect quickly. It would also be possible to bring Child Benefit into taxation though at the expense of some absurdity in receiving benefit with one hand and paying tax on it with the other.

11. There is no need to opt simply for one alternative rather than another. Depending on the Group's reactions, they might wish to have a combination of options explored, eg restricting eligibility to the second and subsequent children, but with means-test access to benefit for the first child, and a small across-the-board real-terms reduction in the value of the benefit.

#### Family Credit

12. Mr Fowler's proposal (para 3 above) is an attempt to direct help to poor working families more effectively than the present FIS. It is proposed to align the eligibility tests and the entitlement with those for supplementary benefit (the Group has agreed a comparable proposal for housing benefit) and it is hoped that making it a credit





(ie. paying it through the wage packet) will have an impact on wage flexibility and readiness to take jobs by improving incentives and reducing the effects of the unemployment and poverty traps. These objectives are laudable. There will however be a net cost (now estimated at £67 million per annum) compared with FIS. Whether this matters significantly will depend on the earlier discussion of savings on child benefit.

#### Benefits in Kind - Welfare Milk and School Meals

13. Mr Fowler proposes to withdraw these benefits but to give compensating cash help (at no net additional cost) to recipients of family credit. A similar change could be made for recipients of supplementary benefit though Mr Fowler does not firmly recommend either for or against this. The difficulty seems to be that there would be losers (because not all those eligible at present take up the benefit). Abolition would be in line with the philosophy of giving those who need it both money and the choice how to use it.

#### HANDLING

14. You may like to say at the outset that overall savings and child benefit might best be discussed first, followed by Family Credit. In that case you should invite the Chief Secretary, Treasury, to introduce his paper on Child Support and the Secretary of State for Social Services to speak to his minute. Most members of the Group will wish to contribute. On Family Support, you should invite the Secretary of State for Social Services to introduce his proposals and Treasury ministers to comment. The Secretary of State for Education and Science may have views, especially on benefits in kind.

#### CONCLUSIONS

You will wish the Group to reach conclusions on :-

- (i) The quantum of savings to be secured in this area;
- (ii) Whether further work should be done on





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- means-testing child benefit
- a reduction in its real value
- restrictions on eligibility
- taxation of child benefit
- alternative tax proposals, eg for a family tax allowance

(iii) whether FIS should be abolished and replaced by Family Credit as proposed by the Secretary of State, in particular with

- eligibility and benefit aligned with supplementary benefit
- payment through the wage packet

and at a net cost of £50-75 million

(iv) whether the benefits in kind (welfare milk and school meals) should be abolished for families on Family Credit and/or on supplementary benefit.

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Cabinet Office  
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