Mr Byatt
Mr Walters

CONFIDENTIAL

Prime Minister
Mr Jenkin is getting cold feet. You may hear more of this from the Small Business Officers tomorrow.
A group of Ministers discussed this tonight, but resolved nothing. The Home Secretary will convene them again on Wednesday.
Do you wish to comment?
MAP 9/2

THE PRIME MINISTER

EMPLOYERS' STATUTORY SICK PAY

1. Our proposals for a scheme for Employers' Statutory Sick Pay are due to be published in a Bill later this week, with Second Reading a fortnight away. The Bill proposes that, apart from reimbursement arrangements for small businesses and in respect of new recruits to an employment, the State should divest itself of any responsibility for payments in respect of up to 8 weeks sickness among employees. Employers would be liable instead for a minimum payment by way of sick pay. They would be compensated for this by a reduction in their national insurance contribution.

2. The CBI have strenuously resisted these proposals, both on the grounds of the extra indirect costs which would be put upon industry (and which would not be met by the contribution reduction) and, more particularly, of the disproportionate cost which would be borne by the manufacturing section of industry where sickness experience is above average. As an alternative, the CBI have pressed for a system whereby employers would be liable for a minimum level of sick pay, which would be fully reimbursed by Government. We have pointed out, however, that full reimbursement to employers, on the basis of individual scrutiny of sickness claims, would be as staff-intensive as current DHSS operations, and the CBI have responded by arguing that employers should be allowed to withhold their sickness payments from the monthly remittances of contributions or tax which they make to Government. This also we have felt bound to reject, on the grounds that employers could not be expected to exercise adequate control over sickness payments for which they were being fully reimbursed by the State.

3. There have been two major recent developments. First, when I met the Party's Small Business Committee last Thursday they urged strongly that any reimbursement to small firms should be on the basis of allowing them to deduct the money due to them from payments to the Inland Revenue (on the lines of the CBI proposal). Any other reimbursement arrangement, which required them to lodge claims before receiving a payment, would be strongly opposed on the grounds of its effect upon cash flow and the

necessary extra paper-work. On the following day, the CBI - having, I believe, heard of this reaction - approached my office with the suggestion that reimbursement to all employers might take the form of making good a proportion, perhaps 50 per cent, of their sick pay liabilities rather than meeting them in full. The remainder of the reimbursement would still be through an adjustment of the national insurance contribution - perhaps 0.3 per cent. Their suggestion (confirmed at a meeting I held with them this morning) was that our acceptance of this alternative approach would considerably lessen hostility to the scheme among their members, and so ease the passage of the Bill.

4. It is very late in the day for us to consider changing course, but nevertheless the attraction of a scheme which would command much greater assent among our supporters in the House and in the country than our original proposals seems to me to be worth consideration. Accordingly, I should be grateful if I could have the guidance of senior colleagues over whether to offer to accept a suitable amendment at the Committee stage of the Bill.

5. The advantages of the modified CBI approach seem to me to be:-

i. since employers would be meeting half the cost of minimum sick pay themselves, they would have a direct financial incentive to challenge doubtful claims, and this would offer some protection to the State;

ii. those industries with a disproportionate amount of sickness would be able to recover half their statutory sick pay costs, which would cushion them against high sickness absence; and

iii. the political prospects of achieving the Bill, without further damaging amendments, would be greatly enhanced.

6. Nevertheless, it must be recognised that there are some major advantages of our present proposals which would be lost if we compromised with the CBI. These are:-

i. we could not expect to achieve the full saving of 5,000 DHSS staff. The effect of having to take account, in the State's financial transactions with every employer, of that employer's individual sickness experience will be bound to mean, however simplified we make our new arrangements, that staff savings would be unlikely to exceed one-half that target;

ii. even the residual staff savings - of perhaps 2,500 - would be further eroded if there were to be any difference of treatment for new employers or for small firms. This would have to be resisted - which could give rise to further criticism from the Small Firms lobby;

iii. the starting date of April 1982 becomes uncertain. We are examining urgently how quickly a revised set of procedures, involving the Inland Revenue, could be introduced but at present it cannot be said with certainty that the original deadline could be met. Possibilities are a postponement until the Autumn of 1982 or until April 1983.

7. It seems to me that the issues are evenly balanced, but an early decision is needed if we are to have any chance - under the original proposals or the alternative - of achieving staff and public expenditure savings in 1982. The postponement of the Bill, pending further consideration, could well mean a year's delay. As I see it, if we can be sure of getting our present proposals through the House without undue loss of Party support in the country, then we should go ahead as planned. If however there is a serious risk that we shall be pushed, either in the Commons or the Lords, to move to the new, Mark II, CBI scheme, I would <u>much</u> rather take the decision now to switch to that and then stick to it, rather than have to give way under pressure. To change during the Committee or Report Stage would be bound to push implementation to 1983. I should be most grateful for colleagues'

guidance, on how we should proceed. Copies of this minute go to Sir Geoffrey Howe, Francis Pym, Christopher Soames, and Michael Jopling.

9 February 1981 P.J.

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Social Service

Treasury Chambers, Parliament Street, SW1P 3AG

Rt Hon Patrick Jenkin MP
Secretary of State
Department of Health and Social Security
Alexander Fleming House
Elephant & Castle
London SE1 8BY

24 March 1981

Dear Patrick

ESSP

I am sorry not to have replied before to your letter of 24 February.

I do not think that I can go along with all your arguments. It is certainly common ground between us that the postponement and partial loss of manpower savings is a serious setback and the small resultant increase in the PSBR is unfortunate. But I think that the setback goes beyond this. Our commitment to the reduction of the public expenditure is not just a means to the end of reducing the PSBR. It is also a means to reducing the scale of the public sector. And it is a major objective in its own right, as the recently published Public Expenditure White Paper and the Chancellor's Budget Speech made clear.

Given this, although exceptions can arise, the fact that a change is virtually PSBR neutral is not a sufficient justification for accepting an increase in, or the avoidance of any reduction in, the total of public expenditure. Admittedly the change to ESSP would not have had much effect on the PSBR, but it will represent the withdrawal of the public sector from involvement in particular flows of funds from employers to employees. It will be a genuine move towards privatisation. Its delay makes it that much harder for us to demonstrate that we are honouring our commitment to reduce the public expenditure total. In its absence, we have got to consider how else we can make that commitment credible.

More generally many proposals which are PSBR neutral involve increasing public expenditure and increasing revenue through a tax or quasi tax. Such proposals would work against at least two of our objectives at the same time.

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

Yours ever
Leon

LEON BRITTAN