PREM 19/185

PART 1 ends:-

ChEx to Ld Pres. 30.6.80

PART 2 begins:-

P/S Env to S/S Scotland 28.11.80

~~HMT (Pensions Inquiry) to TL 3.12.80~~

TO BE RETAINED AS TOP ENCLOSURE

Cabinet / Cabinet Committee Documents

Reference	Date
E(80) 1st Meeting, Item 5	15/01/80
Limited Circulation Annexe, E(80) 1st Meeting	
Minutes, Item 5	15/01/80
E(80) 4	21/01/80
E(80) 2nd Meeting (LCA), Item 2	23/01/80
E(80) 16	18/02/80
E(80) 18	18/02/80
E(80) 7th Meeting, Item 1	20/02/80
Limited Circulation Annexe, E(80) 7th Meeting	
Minutes, Item 1	20/02/80

The documents listed above, which were enclosed on this file, have been removed and destroyed. Such documents are the responsibility of the Cabinet Office. When released they are available in the appropriate **CAB** (CABINET OFFICE) CLASSES

Signed OWayland Date 9 March 2010

PREM Records Team

Enon Pol.

CHANCELLOR OF THE EXCHEQUER

cc Mr Wolfson.

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000 30 June 1980

The Rt Hon Lord Soames, PC, GCMG, GCVO, CBE
Lord President of the Council
Civil Service Department
Whitehall
LONDON SW1A 2AZ

R 3/7

Dear Christopher

PENSIONS ENQUIRY: GOVERNMENT EVIDENCE

I have reflected carefully on the view you expressed in your letter of 23 June. I still feel that we should offer some background explanation on the lines of the paper I sent to you, and it does not seem to me that this will either point the enquiry in the wrong direction, or go unreasonably beyond exposition of the considerations which led to the enquiry.

I can, however, accept all the amendments suggested in the separate letter from your Private Secretary, being in general improvements which I welcome.

.... Accordingly, I am sending an amended version (of which I attach a copy) to the Enquiry. I am sending a copy of this letter and the enclosure to the Prime Minister.

Yours ever

Geoffrey

GEOFFREY HOWE

BACKGROUND TO THE ENQUIRY

The Government's decision to set up this enquiry reflects deep concern, shared by Parliament and much public opinion, over the cost and value of fully inflation-proofed pensions, after the experience of several years of very rapid inflation. The problem is particularly troublesome because full inflation-proofing has been for some years applied generally - and in some important cases statutorily undertaken - for public sector employees; but it has been very rare - and perhaps never guaranteed - in private sector schemes. The differences are underlined by the fact that many public sector schemes are not funded, and where funded have in a few cases been financially assisted by the Government. Private sector schemes have to be commercially operated, may be subsidised in case of difficulty by parent employers, but are more plainly exposed to financial limitations and constraints. Meanwhile the self-employed and others lacking occupational pension schemes are limited to whatever returns they can obtain through use of commercial savings media. This note sets out the background to the Enquiry, and the reasons which led the Government to set it up, without expressing views on the subject matter of the Enquiry.

Information about Pension Schemes

There is a very wide variety of pension schemes, not only in the private sector, but also in the public sector. The great majority, in both public and private sectors, conform to a broad pattern in which a full working career is recognised by the award of a pension of a value around two-thirds salary at or around the close of the career (typically paid in a mixture of immediate lump sum gratuity and subsequent regular pension payments). The many detailed variations of career qualification, method of calculation of the pension in relation to salary, special death, family or other provisions and contribution arrangements reflecting these differences, although important in themselves and in making comparisons, are unlikely to be germane to the object of the enquiry. In general, there are recognised actuarial methods for evaluating such matters and there are no particular differences of technique or approach between public and private sectors.

A good deal of information could readily be supplied about the many public sector schemes, covering some 5 - 6 million present employees (and many of their predecessors, now pensioners) in direct Government service, or employed by local authorities, nationalised industries and other public bodies. It is estimated that some 6 - 7 million employees (and their predecessors, now pensioners) are members of private sector pension schemes. The Government has less comprehensive information about them.

The History of Inflation-Proofing

In the decades before 1970, the practice of awarding pensions in relation to final salary became widespread, with the majority of private pension schemes adopting this principle which had in general already developed in the public sector. It was, however, rare for any systematic provision to be made to maintain the value of pensions after retirement. Subsequent developments in public sector pensions are set out in evidence submitted by the Civil Service Department, which describes the main legislation on which inflation-proofing of "official pensions" is now based.

Other pension schemes in the public sector are not directly governed by this legislation, but the same or similar provisions have in practice been adopted by all under the varying legislation, agreements, pension fund rules, etc., with which they operate. The ability of funded public sector schemes, of which there are many, to meet the commitments involved depends on the management of funds, the willingness and ability of the industry or authority concerned to give any necessary financial support, and in a few cases on assistance from Government.

The practice in private pension schemes varies a great deal. As already mentioned, full inflation-proofing has been rare during the past few years of rapid inflation; and guarantees which could be regarded as the equivalent of the statutory commitment in relation to some parts of the public sector are unknown. Nevertheless, many private pension schemes have recognised the problems of declining value of pensions and have adopted one, or often a combination, of two approaches:

- a guaranteed regular annual enhancement of pensions, typically of the order of 3 per cent per annum; and

- discretionary enhancement at annual or less frequent intervals, depending on experience of inflation, on the state of the pension funds and frequently on the willingness of the parent employer to provide financial support to strengthen the funds.

Comprehensive information is not available about how much pensions have in practice been increased. But the review by the Government Actuary in the course of the 1980 Civil Service pay research exercise indicated that the analogue employers (excluding those providing full index-linking automatically or with no provision for discretionary increases) had on average increased pensions in payment by between 50 and 55 per cent of the actual increase in the cost of living over the previous five years. In that period, prices approximately doubled, so that, on average, pensions had lost value to the tune of 20 - 25 per cent.

Relevance of State Pension Schemes

Present State Pension Scheme arrangements go back to the Social Security Pensions Act 1975 and the Social Security Act 1975, which have an important bearing on the subject, particularly for the future. This legislation provides for a flat-rate basic State pension and, for employees, an earnings-related additional pension. The earnings-related additional pension is related to an individual's earnings up to a limit - about one and a half times average earnings - in each tax year from 1978-79. The amount payable by way of additional pension under the State schemes will be based on the best 20 years of earnings in a person's working life from 1978-79, revalued in line with the historic movement of average earnings over the period. The amounts awarded by way of additional pension will initially be relatively small but will build up over the first 20 years of the scheme.

Employers with occupational pension schemes which provide pensions at least as good as the State earnings-related additional pension can contract out of the scheme. Public service pensioners generally are contracted out. People contracted-out of the State scheme receive the State basic pension however.

The Social Security Acts provide for the basic and earnings-related additional State pensions to be increased annually at least in line with prices. (Prior to 1980, the basic pension had to be increased in line with earnings or prices, whichever was the more advantageous.) Other occupational schemes are not required to inflation-proof their pensions but the State pension payable to people who have been contracted-out is increased to inflation-proof that part of the occupational pension which corresponds to the earnings-related additional State pension which would have been payable if the employee has not been contracted-out. On this basis, in just under 20 years, basic State pensions and, as far as employees are concerned, an additional earnings-related pension either from the State or from an occupational pension scheme will effectively be guaranteed on an inflation-proofed basis throughout the community. The inflation-proofing of occupational pensions other than public service pensions will however only be guaranteed up to a certain level as indicated above. In the case of a married man on average earnings these provisions will provide inflation-proofed pensions for him and his wife totalling about half-pay.

The Impact of Recent Developments

Provisions in private pension schemes of the kinds described immediately above were introduced against the background of persistent inflation at a rate of a very few percentage points annually, in line with experience before the past decade. They might well have been adequate to secure maintenance of value of pensions during retirement. It is indeed likely that the implicit expectation of this underlay the general public acceptance and all-Party support in Parliament when the 1971 provisions for regular inflation-proofing of many public service pensions were enacted.

A totally different situation arose with the very rapid inflation of the 1970's accompanied by a persistent decline in rates of return on investment in real terms. Many private pension funds needed to call on parent employing companies to augment their financial resources on actuarial advice. Within the limits of such financial strengthening as could be obtained, full maintenance of value of pensions after retirement was rarely possible and the cumulative effect of several years of unfavourable experience has resulted in very large discrepancies between the initial and current value of a high proportion of pensions under private schemes. Even more marked has been the erosion of value of annuities and investment yields available to those relying on commercial savings media. This has in turn meant that the discrepancy in treatment of those retiring from public and private employment has grown rapidly, and that public attention and criticism has focussed on this sharply. Criticism is addressed to the problems of: the cost of inflation-proofing of public sector pensions; the special value of security of pensions value enjoyed by public sector pensioners; and the question whether these costs and values are adequately reflected in employee contributions and overall remuneration in the public sector. These points are dealt with in the following sections of this note.

The Problem of Cost

A good deal of work is done in the public sector on actuarial costing of inflation-proofed pensions. The contributions to nationalised industry pension funds are based on costings which include inflation-proofing and, within the public service, the Governmen Actuary undertakes regular costings of the teachers' and NHS notional funds, in which he considers it right to draw attention to the accruing liability for inflation-proofing.

The most systematic and frequent costing in the public sector is that done by the Government Actuary in relation to the Civil Service scheme. This is also the most systematic attempt to relate the total cost-including inflation-proofing - to what the employee pays, through the pension deduction applied to the non-industrial Civil Service. (During the past year or so, a similar concept has been applied to certain other public service employees.)

Separate notes are being submitted; by the Civil Service Department explaining the principle of comparison which is the basis for determining overall remuneration of the non-industrial Civil Service; and by the Government Actuary explaining how he makes the pension calculations which are then incorporated in Civil Service pay determination.

The methods adopted by the Government Actuary - indeed the whole process - have come under criticism. There was discussion of this, now in some respects out of date, in Chapter VI of the Eleventh Report from the Expenditure Committee of the House of Commons, published 25 July, 1977. The enquiry team will want to examine carefully the approach adopted by the Government Actuary, who will be able personally to supplement the published information already available in the sequence of reports he has made in relation to successive Civil Service pay settlements.

The Problem of Value

In principle, the approach enshrined in the arrangements for handling Civil Service pay aims to cost the net additional benefits of Civil Service pensions on an appropriate comparison, and then charge the employees in the Civil Service a corresponding contribution (through notional deduction from salary), so that the total package of remuneration for the civil servant and for the outside employee with whom he is compared is the same, taking career service and pension into account together. It must be for consideration, however, whether this concept, however accurately the costing is done, adequately incorporates the value to the recipient of an inflation-proofed pension. The essence of the problem is one of security. In theory, the public servant has no absolute guarantee of an inflation-proofed pension, because it can be revoked by Parliament at any time, and no Parliament can bind its successors. However, the public servant is perceived - and may perceive himself - to have a degree of security which is not available elsewhere. Many members of private pension schemes might be eager to obtain such security, by the payment of a higher pension contribution during their working careers, if the opportunity were available to them: in practice it is not so available because, although many private schemes have accepted inflation-proofing up to retirement, by linking pension awards to final salary, post-retirement inflation-proofing is not offered. The important question is whether the security conferred by full inflation-proofing should be regarded as having a value to the potential beneficiaries over and above any average actuarial cost.

Conclusion

The appraisal of any additional value to the potential beneficiary of the security of inflation-proofing cannot be carried out by straightforward objective calculation. This is an area in which judgment is needed, and this enquiry has been established in the hope of obtaining such judgment.

Attention has been focussed in this note on the non-industrial Civil Service, solely because that is an area in which an explicit attempt has been made, at least partially, to tackle the problem of the cost and value of inflation-proofing. In other areas of the public sector, there is a wide variety of contributory and non-contributory arrangements, with or without further notional account taken of pension values in determining pay, and in most of these other areas the present arrangements go back in history some years and have not been adjusted during the last few years. It is the Government's intention, in the light of the findings of this enquiry, to reconsider present arrangements for public sector pensions generally. It cannot be clear in advance whether extensive changes will be thought appropriate, or whether such changes would be more appropriately made in the structures of pension schemes, contribution arrangements, or pay determination, or through different methods in different cases. Any future proposals on these lines will of course be matters for careful discussion, and where appropriate negotiation, by the managements and staff associations and unions concerned.

The close connection between pay and pensions as part of overall remuneration is obvious. To the extent that any changes may be desirable, the Government would like to be in a position to embark on them as soon as possible, and has asked that the enquiry should be completed within a short space of time so that its findings can be available well in advance of the major public sector pay negotiations of 1981.

H.M. TREASURY

30 June, 1980

Econ Pol.

LORD PRESIDENT OF THE COUNCIL

Civil Service Department
Whitehall London SW1A 2AZ
01-273 4400

23 June 1980

The Rt Hon Sir Geoffrey Howe, QC, MP
Chancellor of the Exchequer
HM Treasury
Parliament Street
LONDON SW1P 3AG

Dear Geoffrey,

PENSIONS ENQUIRY: GOVERNMENT EVIDENCE

Thank you for your letter of 13 June enclosing a draft paper to the enquiry.

This exercise offers us an opportunity to make substantial savings on the public sector pay bill. Simply raising the contributions paid by local government employees, teachers, NHS workers, and so on, to the level paid by the Civil Service could raise £¼ billion a year. Every 1% contribution on top of that may raise another £200 million. But if there is to be a real chance of achieving these savings Sir Bernard Scott's recommendations must carry credibility, in particular with the public sector unions. They will not do so if we point the Enquiry in the wrong direction.

Having given Sir Bernard Scott explicit terms of reference we should surely leave him to get on with the job and not lean on him as does your draft paper. There are of course many difficulties in the costing of pensions and these will have to be faced by Sir Bernard Scott and his colleagues. I see no reason to direct him away from them. What we must do is to encourage the enquiry to do their job thoroughly and to support their conclusions with reasoned arguments. This is essential if they are to carry conviction and achieve the right result.

I therefore see no need for your suggested paper and I would prefer it not to go forward but if you feel strongly about it I would want to make a number of detailed points on your draft.

I am sending a copy of this to the Prime Minister.

Yours ever
Christopher

SOAMES

23 JUN 1980

Econ Pol

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

NBPM yet

13 June 1980

R 20/6

The Rt. Hon. Lord Soames, PC, GCMG, GCVO, CBE
Lord President of the Council

Dear Christopher

PENSIONS ENQUIRY : GOVERNMENT EVIDENCE

The Scott Enquiry into the Value of Pensions, etc. is about to begin its work. Our officials have been in touch with each other about initial papers which might be put in as background evidence by the Government.

I see no problem about three of the areas which it is proposed to cover in separate papers: I understand that your people are preparing a factual paper on public sector pension arrangements and another explaining the system of comparability and pay research and how the treatment of pensions fits into it; and the Government Actuary is preparing a paper describing his approach to the problem and the role he plays in valuing the pensions component for Civil Service (and now some other) pay determination. All these seem necessary and, as they are basically factual, should cause us no particular difficulty. I have in fact asked if I could see the individual papers before they are presented, which will help me to keep track of the points put to the Enquiry on behalf of the Government.

I believe there is a need, however, for a further paper, rather less factual, giving some indication of the reasons why we have set up this Enquiry, and some pointers to the directions which we would like the Enquiry to take. We must obviously avoid being too tendentious, and we do not indeed have definitive views to offer. I
..... have had the attached draft prepared, which I think gives the right kind of steer, without pre-empting discussion which the members of the Enquiry team must themselves

/pursue.

pursue. I understand that your officials have some hesitation about the desirability of putting in a paper of this kind at all, and that they feel that the emphasis is in some respects misplaced. I hope you will agree with me that the draft does reasonably reflect the direction of enquiry we are looking for and that we should submit it.

I am copying this letter and enclosure to the Prime Minister. I have not felt it necessary to draw in a wider group of colleagues and would be glad to know whether the Prime Minister feels that we should do so.

GEOFFREY HOWE

BACKGROUND TO THE ENQUIRY

The Government's decision to set up this enquiry reflects deep concern, shared by Parliament and much public opinion, over the cost and value of fully inflation-proofed pensions, after the experience of several years of very rapid inflation. The problem is particularly troublesome because full inflation-proofing has been for some years applied generally - and in some important cases statutorily undertaken - for public sector employees; but it has been very rare - and perhaps never guaranteed - in private sector schemes. The differences are underlined by the fact that many public sector schemes are not funded, and where funded have in a few cases been financially assisted by the Government; whereas private sector schemes have to be commercially operated, may be subsidised in case of difficulty by parent employers, but are more plainly exposed to financial limitations and constraints. This paper sets out the background to the Enquiry, and the reasons which led the Government to set it up, without expressing views on the subject matter of the Enquiry.

Information about Pension Schemes

There is a very wide variety of pension schemes, not only in the private sector, but also in the public sector. The great majority, in both public and private sectors, conform to a broad pattern in which a full working career is recognised by the award of a pension of a value around two-thirds salary at or around the close of the career (typically paid in a mixture of immediate lump sum gratuity and subsequent regular pension payments). The many detailed variations of career qualification, method of calculation of the pension in relation to salary, special death, family or other provisions and contribution arrangements reflecting these differences, although important in themselves and in making comparisons, are unlikely to be germane to the object of the enquiry. In general, there are recognised actuarial methods for evaluating such matters and there are no

/particular

particular differences of technique or approach between public and private sectors. Similarly, it may well be unnecessary for the purposes of the enquiry to explore in detail the wide variety of contribution and financial management arrangements, again with much variety in the public sector as well as in the private sector, where such details do not bear on the objects of the enquiry.

A good deal of information could readily be supplied about the many public sector schemes, covering some 5 - 6 million present employees (and many of their predecessors, now pensioners) in direct Government service, or employed by local authorities, nationalised industries and other public bodies. It is estimated that some 6 - 7 million employees (and their predecessors, now pensioners) are members of private sector pension schemes. The Government has less comprehensive information about them.

The History of Inflation-Proofing

In the decades before 1970, the practice of awarding pensions in relation to final salary became widespread, with the majority of private pension schemes adopting this principle which had in general already developed in the public sector. It was, however, rare for any systematic provision to be made to maintain the value of pensions after retirement.

Nevertheless, the main groups of pensions of employees in direct Government service, and some other public sector pensioners, enjoyed periodic adjustments through special Pensions Increase Acts. Adjustments tended to reflect increases in the cost of living at a time when inflation was persistent, but at a fairly modest annual rate.

/In 1971.

In 1971, the first major step was taken towards systematic arrangements. Provision was made, in relation to a major group of public service pensions (including civil servants, ministers and members of parliament, the judiciary, police and firemen, teachers, health service employees, local authority employees and some others) for a regular 2-yearly review and adjustment to reflect a substantial intervening increase in the cost of living. These initial arrangements were developed in stages to the present system, which is built into the Social Security Act of 1975 and the Social Security Pensions Act of 1975, and requires that official pensions be increased by the same percentage as the increase of the additional earnings-related pension, which in turn has to be increased annually at least in line with prices.

Other pension schemes in the public sector are not directly governed by this legislation, but the same or similar provisions have in practice been adopted by all under the varying legislation, agreements, pension fund rules, etc., with which they operate. The ability of funded public sector schemes, of which there are many, to meet the commitments involved depends on the management of funds, the willingness and ability of the industry or authority concerned to give any necessary financial support, and in a few cases on assistance from Government.

The practice in private pension schemes varies a great deal. As already mentioned, full inflation-proofing has been rare during the past few years of rapid inflation; and guarantees which could be regarded as the equivalent of the statutory commitment in relation to some parts of the public sector are unknown. Nevertheless, many private pension schemes have recognised the problems of declining value of pensions and have adopted one, or often a combination, of two approaches:

- a guaranteed regular annual enhancement of pensions, typically of the order of 3 per cent per annum; and

/- discretionary

- discretionary enhancement at annual or less frequent intervals, depending on experience of inflation, on the state of the pension funds and frequently on the willingness of the parent employer to provide financial support to strengthen the funds.

Relevance of State Pension Schemes

Present State Pension Scheme arrangements go back to the Social Security Pensions Act 1975 and the Social Security Act 1975, which have an important bearing on the subject, particularly for the future. This legislation provides for a flat-rate basic State pension and, for employees, an earnings-related additional pension. The earnings-related additional pension is related to an individual's earnings up to a limit - about one and a half times average earnings - in each tax year from 1978-79. The amount payable by way of additional pension under the State schemes will be based on the best 20 years of earnings in a person's working life from 1978-79, revalued in line with the historic movement of average earnings over the period. The amounts awarded by way of additional pension will initially be relatively small but will build up over the first 20 years of the scheme.

Employers with occupational pension schemes which provide pensions at least as good as the State earnings-related additional pension can contract out of the scheme. Public service pensioners generally are contracted out. People contracted-out of the State scheme receive the State basic pension however.

The Social Security Acts provide for the basic and earnings-related additional State pensions to be increased annually at least in line with prices. (Prior to 1980, the basic pension had to be increased in line with earnings or prices, whichever was the more advantageous.) Other occupational schemes are not required to inflation proof their pensions

/but the State

but the State pension payable to people who have been contracted-out is increased to inflation-proof that part of the occupational pension which corresponds to the earnings-related additional State pension which would have been payable if the employee has not been contracted-out. This means that in just under 20 years, basic State pensions and, as far as employees are concerned, an additional earnings-related pension either from the State or from an occupational pension scheme will effectively be guaranteed on an inflation-proofed basis throughout the community. The inflation-proofing of occupational pensions other than public service pensions will however only be guaranteed up to a certain level as indicated above. In the case of a married man on average earnings these provisions will provide inflation-proofed pensions for him and his wife totalling about half-pay.

The Impact of Recent Devleopments

Provisions in private pension schemes of the kinds described immediately above were introduced against the background of persistent inflation at a rate of a very few percentage points annually, in line with experience before the past decade. They might well have been adequate to secure maintenance of value of pensions during retirement. It is indeed likely that the implicit expectation of this underlay the general public acceptance and all-Party support in Parliament when the 1971 provisions for regular inflation-proofing of many public service pensions were enacted.

A totally different situation arose with the very rapid inflation of the 1970's accompanied by a persistent decline in rates of return on investment in real terms. Many private pension funds needed to call on parent employing companies to augment their financial resources on actuarial advice. Within the limits of such financial strengthening as could be obtained, full maintenance of value of pensions after retirement was rarely possible and the cumulative effect of several years of unfavourable experience has resulted in

/very large

very large discrepancies between the intial and current value of a high proportion of pensions under private schemes. This has in turn meant that the discrepancy in treatment of pensioners from public and private employment has grown rapidly, and that public attention and criticism has focussed on this sharply. Criticism is addressed to the problems of: the hidden cost of inflation-proofing of public sector pensions; the special value of security of pensions value enjoyed by public sector pensioners; and the question whether these costs and values are adequately reflected in employee contributions and overall remuneration in the public sector. These points are dealt with in the following sections of this note.

The Problem of Cost

It seems unlikely to be fruitful to attempt to establish the cost of inflation-proofing by examining actual experience in public sector schemes which operate it. Apart from the confusion of evidence from different financing arrangements, current pension payments merely reflect developments over one particular period in respect of a population in most cases very different from the present working population; where pension funds are used, valuations and revaluations in response to changing circumstances may vary.

The one case in which a systematic attempt at costing has been made in the public sector is the work over several years of the Government Actuary in relation to the notional pension contribution (applied in the form of a notional deduction from salary) for the non-industrial Civil Service. (During the past year or so, a similar concept has been applied to certain other public service employees.)

Separate notes are being submitted: by the Civil Service Department explaining the principle of comparison which is the basis for determining overall remuneration of the non-industrial Civil Service; and by the Government Actuary explaining how he makes the pension calculations which are

/then incorporated

then incorporated in Civil Service pay determination.

The methods adopted by the Government Actuary - indeed the whole process - have come under criticism. There was discussion of this, now in some respects out of date, in Chapter VI of the Eleventh Report from the Expenditure Committee of the House of Commons, published 25 July 1977. The enquiry team will want to examine carefully the approach adopted by the Government Actuary, who will be able personally to supplement the published information already available in the sequence of reports he has made in relation to successive Civil Service pay settlements.

The Problem of Value

In principle, the approach enshrined in the arrangements for handling Civil Service pay aims to cost the net additional benefits of Civil Sercice pensions on an appropriate comparison, and then charge the employees in the Civil Service a corresponding contribution (through notional deduction from salary), so that the total package of remuneration for the civil servant and for the outside employee with whom he is compared is the same, taking career service and pension into account together. It must be for consideration, however, whether this concept, however accurately the costing is done, adequately incorporates the value to the recipient of an inflation-proofed pension. The essence of the problem is one of security. Where inflation-proofing is guaranteed, the pensioner has no worry on this score, whatever the contribution he may have paid during his working life, and whatever adverse developments may take place in the rate of inflation or the return on investments during his life-time. Many members of private pension schemes might be eager to obtain such security, by the payment of a higher pension contribution during their working careers, if the opportunity were available to them: in practice it is not so available because, although many private schemes have accepted inflation-

/proofing up

proofing up to retirement, by linking pension awards to final salary, post-retirement inflation-proofing is not offered. The important question is whether the security conferred by full inflation-proofing should be regarded as having a value to the potential beneficiaries over and above any average actuarial cost.

Conclusion

It seems that neither the attempt to establish an actuarial relative cost of inflation-proofing, nor the appraisal of any additional value to the potential beneficiary of the security of inflation-proofing, can be carried out by straightforward objective calculation. Both are areas in which judgment is needed, and this enquiry has been established in the hope of obtaining such judgment.

Attention has been focussed in this note on the non-industrial Civil Service, solely because that is an area in which an explicit attempt has been made, at least partially, to tackle the problem of the cost and value of inflation-proofing. In other areas of the public sector, there is a wide variety of contributory and non-contributory arrangements, with or without further notional account taken of pension values in determining pay, and in most of these other areas the present arrangements go back in history some years and have not been adjusted during the last few years. It is the Government's intention, in the light of the findings of this enquiry, to reconsider present arrangements for public sector pensions generally. It cannot be clear in advance whether extensive changes will be thought appropriate, or whether such changes would be more appropriately made in the structures of pension schemes, contribution arrangements, or pay determination, or through different methods in different cases. Any future proposals on these lines will of course be matters for careful discussion, and where appropriate negotiation, by the managements and staff associations and unions concerned.

/The close

The close connection between pay and pensions as part of overall remuneration is obvious. To the extent that any changes may be desirable, the Government would like to be in a position to embark on them as soon as possible, and has asked that the enquiry should be completed within a short space of time so that its findings can be available well in advance of the major public sector pay negotiations of 1981.

cc csd rh
doe
Econ Pol

C.F. Original - AR

10 DOWNING STREET

THE PRIME MINISTER

11 June 1980

Dear Nicholas

Thank you for your letters of 21 May to Paul Channon and me enclosing one, which I now return, from your constituent Mr P G Taylor of 7 Badger Road, Prestbury about the inquiry into the value of pensions.

I announced the inquiry's membership and terms of reference by Written Answer to Robert Dunn on 22 May and I enclose a copy of the Hansard report. As Mr Taylor will see, the inquiry is intended to consider the extent to which the value of pensions is taken into account in setting the levels of public sector pay. It is, of course, for the inquiry to decide what specific points they wish to examine. The terms of reference are, however, concerned with the valuation of the inflation-proofing of pensions in the public sector and the contributions paid for this benefit by existing employees. The inquiry is not specifically concerned with the pensions paid to particular groups of current pensioners.

Mr Taylor's letter does not enable me to say with any certainty what are the precise reasons for the depressed value of his basic pension. This may have been due to a staged pay award, or it may have been a residual effect of the final stages of the last Government's incomes policy. It is not, of course, unusual for people to have to retire shortly before a major pay award, so that their pensionable pay is lower than it might have been had they stayed on for a few more months. This effect was, however, particularly acute towards the end of the last incomes policy.

/After

After very careful and sympathetic consideration the Government have concluded with regret that we could not make a general improvement to the position of those affected in this way by incomes policy - primarily because of the formidable cost of any remedial measures. We have estimated, for example, that the cost of one limited form of improvement would be of the order of £100 million a year. Nevertheless, Mr Taylor may be interested to know that the Government have indicated that, in the case of some staged pay awards, they would not object to the retrospective promulgation of notional rates of pay for pension purposes. I cannot say whether Mr Taylor would be likely to benefit from this, and I should not like to raise his hopes prematurely. But I would suggest that he makes enquiries of his former employers to find out whether they are contemplating such measures and, if so, what his own position is likely to be.

Signed

MT

Nicholas Winterton, Esq MP

Econ Pol

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

29 May 1980

The Rt Hon Lionel Murray OBE
General Secretary
Trades Union Congress
Congress House
Great Russell Street
London WC1B 3LS

Dear Len

PUBLIC SERVICE PENSIONS

Thank you for your letter of 22 May. You will perhaps have seen that details of the proposed enquiry were announced on the day on which you wrote to me. I attach a copy of the text of the announcement made by the Prime Minister in answer to a question in the House of Commons, giving the full terms of reference and the membership of the enquiry team.

attached.

As you will recognise, the subject is one of very wide interest, to the Government, Parliament and the public generally, as well as to managements and unions involved in pension arrangements which offer inflation-proofing. Given the nature of the enquiry, the Government did not think it necessary to consult particular interests at this stage. Any interested parties will now have the opportunity of making representations, and you will note that the findings which result from the enquiry will need in due course to be considered, and any consequent proposals discussed or negotiated, by the managements and unions or staff associations concerned.

Yours ever

Geoffrey

GEOFFREY HOWE

Published Papers

The following published paper(s) enclosed on this file have been removed and destroyed. Copies may be found elsewhere in The National Archives.

House of Commons Hansard	22 May 1980
Public Sector Employees (Pay)	Columns 285-288

Signed C Wayland Date 9 March 2010

PREM Records Team

C

TRADES UNION CONGRESS

CONGRESS HOUSE · GREAT RUSSELL STREET · LONDON WC1B 3LS

Telephone 01-636 4030 *Telegrams* TRADUNIC LONDON WC1

LM

YOUR REFERENCE

OUR REFERENCE LM/BC/AC/HKY

DEPARTMENT Economic

st 27/5

May 22 1980

Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer
HM Treasury
Treasury Chambers
Parliament Street
London SW1P 3AG

CH/EXCHEQUER
REC. 27 MAY 1980
ACTION MR LITTLER
COPIES TO CST, FST, MST C, MST L, SIR D. WASS, SIR A. RAWLINSON, MR BAILEY, MR KEMP, MR UNWIN

Dear Sir Geoffrey

Public Service Pensions

At their recent meeting the Public Services Committee of the TUC considered the subject of public service pensions in the light of the reference you made in your Budget speech to setting up an inquiry into index linking of pensions throughout the sector.

This is clearly a matter of direct concern and considerable importance to all unions with membership in the public services, but there appears to be no evidence of any consultation with unions on the establishment, terms of reference or composition of such an inquiry.

The Committee therefore decided that they should, on behalf of public service unions, seek consultation on the terms of reference of the inquiry and, if it is to proceed, adequate representation on it. I am writing to inform you of the Committee's views, and look forward to a constructive response.

Yours sincerely

Lionel Murray

General Secretary

CONFIDENTIAL

Econ Pol

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000
19th May, 1980

T.P. Lankester, Esq.,
Private Secretary,
10, Downing Street

cc Mr Ingham

We decided that this would go out at 3.30 pm. Thursday. I assume CSD have come into line on their two reports.

TL
20/5

Dear Tim,

ENQUIRY INTO VALUE OF PENSIONS

The arrangements for setting up this enquiry, which was briefly foreshadowed in the Chancellor's Budget Speech, have now been settled, and, as we agreed, details are to be announced by Prime Minister's arranged Answer and No.10 Press Notice, on the afternoon of Thursday, 22nd May.

I am copying this letter to the Private Secretaries of all Members of Cabinet, and of the Minister of Transport, Minister of State (CSD), and the Secretary of the Cabinet, and am enclosing with their copies a set of the papers we have prepared for the announcement: the Parliamentary Question and Reply, Terms of Reference, Draft Press Notice, Background Brief for Press Offices, and Brief Notes on the five members of the enquiry team.

Given that the announcement will be made from No.10, and reference is made to the Secretary at the Treasury address, I imagine that most immediate press questioning and public enquiries will come to you or to us. But there is likely to be a good deal of interest in the enquiry on the part of managements and unions of all kinds of public sector bodies whose normal contacts will be in other departments and who may therefore put questions to their usual contacts. The Private Secretaries to whom I am copying this letter may therefore like to pass the contents on immediately, both to their own Press Offices, and to officials who would be the natural point of contact for any outside bodies which normally approach Government through them. Indeed, in a few cases where officials know that the bodies concerned are particularly interested in the subject, they may like to have discretion to give very brief advance notice to them.

/In handling

In handling any questions, particularly from managements and unions in the public sector, it will be important to emphasise the limited subject of the enquiry (see general comment in Background Brief) and the point emphasised in both Parliamentary Answer and Notes for Editors, that any proposals which the Government and other public sector authorities may decide to put forward when the present enquiry has been completed and its findings considered will be a matter for discussion between managements and unions and staff associations concerned.

I am also sending copies of the enclosures, on a personal basis, to members of the Inquiry.

Yours ever,

MH

M.A. HALL

cc Private Secretaries to Cabinet Ministers
PS/ Minister of Transport
PS/ MST(CSD)
PS/ Sir R. Armstrong

Economic Pol.

cc Mr Ingham

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

~~14~~ 15 May 1980

T. Lankester, Esq.,
No.10, Downing Street

Dear Tim,

INDEPENDENT ENQUIRY ON INDEX-LINKED PENSIONS

... As promised, I enclose the remaining two biographical notes to be annexed to the background briefing.

I am copying this letter, with enclosures to Richard Dykes and Geoffrey Green.

Yours ever,

MAH

M.A. HALL

GAVIN LAIRD

Born 14 March 1933

Joined Amalgamated Engineering Union at age of 16

Shop Steward then Convenor with Singer Manufacturing (UK)

1973-75	General Council STUC
1975 -	Executive Councilman for Scotland and North West England
1976-79	General Purposes Committee, TUC
1979 -	Elected Member of TUC General Council
1974-79	Scottish Industries Development Advisory Board Member
1979 -	Member of IDAB
1973-75	Member, Scottish Oil Development Council
1974-75	Member HIDB
1976 -	Part time Director BNOC
1976 -	Member BBC Consultative Group on Industrial and economic affairs
1979 -	Member, Iron and Steel Training Board

SIR BERNARD SCOTT, Kt

Born: 1914

FEng, FIMechE, FBIM, FRSA

Served 1939-45 War (despatches 1944); Belgian Croix de Guerre 1945. 1931 joined Joseph Lucas Limited as apprentice. Held various managerial posts in Lucas companies at home and abroad.

1969-73 Deputy Chairman Lucas Industries Limited

1973-74 Managing Director

1974-80 Chairman

1974 CBE

Director Lloyds Bank Ltd., Lloyds Bank International, Boots, Thomas Tilling.

Member: CBI Council 1974-76

British Overseas Trade Board 1973-77

Vice President: SMM & T 1976 -

Hon LLD Birmingham, 1977

Hon DSC Aston, 1979

BK

hcc: B. Ingham

File

10 DOWNING STREET

From the Private Secretary

14 May 1980

Enquiry into the Value of Pensions

Thank you for your letter of 13 May. The Prime Minister is content to go ahead on the basis proposed, except that she has decided it would be best to announce the enquiry on Thursday 22 May, which is the day the PRU Board report and the Government Actuary's report will be published.

I am sending copies of this letter to Richard Dykes (Department of Employment) and Geoffrey Green (Civil Service Department).

T. P. LANKESTER

Martin Hall, Esq.,
HM Treasury

1

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

13th May, 1980

cc Mr Leigh-Pemberton

Prime Minister

We recommend that the pension enquiry be announced next Thursday (not this Thursday) along with the publication of the PRU Board report and the Government Actuary's report.

T. Lankester, Esq.,
Private Secretary,
10, Downing Street

Dear Tim,

ENQUIRY INTO THE VALUE OF PENSIONS

As I told you on the telephone, we now have a full team, including Gavin Laird. I enclose fair copies of the proposed draft written question and answer, which we agreed could appropriately be tabled for a reply on Thursday. Also attached are the draft press notice, background brief, and short biographical notes on some of the members of the enquiry. I will forward the remaining biographical notes in time for your press release.

As soon as you can confirm the final texts, and that the announcement will definitely be made on Thursday, I should like to write to the Private Secretaries to other members of the Cabinet, and to the members of the enquiry themselves, with copies of the proposed reply and press notice.

I am copying this letter to Richard Dykes and Geoffrey Green.

Yours ever,

M.A. HALL

Better to get them all out on the same day. We have ~~already~~ seen the draft Answer and press notice, which are OK.

Content to go ahead on this basis?

TL. 13/5

Yes [illegible]

Question: To ask the Prime Minister if she is satisfied that the value of index-linked pensions for public sector employees is adequately taken into account in contributions and levels of pay.

Draft Reply: Arrangements in different parts of the public sector vary widely and I am not satisfied that the difficult problem of the value of index-linked pensions has been adequately considered in all of them.

I am therefore setting up an independent enquiry to consider and advise on how such pensions might be valued. Sir Bernard Scott has agreed to be Chairman. Other members will be Sir Alex Jarratt, Professor Harold Rose, Mr Robert E Macdonald and Mr Gavin Laird.

It is my hope that the enquiry can be completed within three or four months. I am sure it will want to consider representations both from those directly concerned and from others. It would then be for the Government and other public sector authorities to decide, in the light of the advice given, whether and what changes in present arrangements would be desirable. Any such changes would of course have to be considered by the managements and unions and staff associations concerned.

The full terms of reference will be as follows:

[Take in text of terms of reference].

TERMS OF REFERENCE

Having regard to the need to ensure that full account is taken in all areas of the public sector, whether by contributions or salary abatement, of the value of inflation-proofing of occupational pensions, and of relative job security, taking due account of arrangements in the private sector:

(a) to consider the assumptions and methods used by the Government Actuary where he assesses the value of differences in inflation-proofing of occupational pensions;

(b) to consider the relative degree of security in the full inflation-proofing enjoyed by public sector employees compared with those in the private sector, and the additional value to be placed upon it;

(c) to consider how to assess the relative job security enjoyed by employees in the private and public sectors;

(d) to report their findings and suggest what valuations or methods of valuation would be appropriate to take account of these factors in determining pay and other conditions of service.

DRAFT PRESS NOTICE

ENQUIRY INTO VALUE OF PENSIONS

The Prime Minister gave the following reply today to a Parliamentary Question about the value of index-linked pensions for public sector employees:

"[Take in text of reply]".

Any correspondence about the enquiry should be addressed to The Secretary, Enquiry into Value of Pensions, c/o H.M. Treasury, Parliament Street, SW1P 3AG.

NOTES FOR EDITORS

This is the enquiry which was also mentioned in the Chancellor's Budget Speech.

2. The Government is concerned about the arrangements for index-linked occupational pensions almost throughout the public sector, which are not matched by occupational pensions in the private sector. The difference of pension treatment and its cost has become important as a result of several years of high rates of inflation, and has attracted strong criticism. The Government is dedicated to the objective of reducing inflation, and success in that will diminish the problems arising from difference kinds of pension treatment.

3. But widespread doubts have been expressed about the valuation of the benefit of index-linking and the Government wishes to explore thoroughly the question whether the additional advantages of index-linked pensions can be adequately valued, and their additional value translated into an appropriate level of contributions or reflected in the settlement of pay. The purpose of the proposed enquiry is to seek advice on the problem of valuation. It would then be for the Government and other public sector authorities to decide, in the light of the advice given, whether and how changes in present arrangements should be made, in consultation with unions and staff associations.

/4.

4. The terms of reference specify two particular elements in valuation which seem to be worth attention: first, one which arises only where (as in the case of the non-industrial Civil Service and some other public service groups) a deliberate attempt is made to cost the effect of inflation-proofing for future years; the other an attempt to get at the elusive problem of valuing security in an uncertain world.

5. The terms of reference also refer to the problem of relative job security. This is of course separate from the pensions valuation problem, but could involve some similar considerations. It has been included in the hope that the enquiry might, in the course of considering security of pensions value, develop ideas which could help in considering job security also.

BACKGROUND BRIEF

General Comment

It is important to emphasise that the enquiry is addressed to the general issue of valuation. It is not being asked to examine in detail the precise arrangements and commitments of existing pension schemes, far less to set out any blue-print of how such schemes might be changed.

For this reason, it should not be necessary for the enquiry to take extensive and detailed evidence in respect of the whole range of public sector pension schemes, which have many important differences of history, statutory or other basis, financial structure and details of calculation of benefits, and contributions.

Continuation of Index-Linking

The enquiry is concerned with the valuation of index-linking, not with the appropriateness of index-linking itself. Pension schemes and the benefits attached to them involve long-run expectations and commitments which should not lightly be interfered with. The Government is conscious of the obligations it has inherited towards its own direct employees and other employees in the public sector. Nevertheless, any Government must ultimately reserve the right to reconsider the arrangements for full inflation-proofing of public sector occupational pensions against the background of national economic and social considerations.

Representations

The Chairman of the Enquiry will no doubt publicise soon his proposals to receive any representations. Meanwhile any comments addressed to The Secretary, Enquiry into Value of Pensions, c/o H.M. Treasury, Parliament Street, London, SW1P 3AG, will be acknowledged and forwarded to the Chairman.

What Public Sector Pension Schemes are Index-Linked?

Nearly all, which makes a very long list, including Civil Service, Ministers, Members of Parliament, Judiciary, Armed Forces, Police, Nurses, Doctors, Teachers and other local authority and nationalised industry employees. In total, some 5½ million present employees in the public sector are covered by index-linked pension schemes.

/Details

Details of Schemes

Details vary, and enquiries should be referred to the managements of the particular public sector groups concerned.

Basis of Present Index-Linking

A large collection of "official pensions", mainly but not exclusively central and local government employees, are covered by the 1971 Pensions (Increase) Act, read in conjunction with other pensions legislation, notably the Social Security Pensions Act 1975. Official pensions are increased in line with forecast movements of the retail price index, at the same time and by the same amount as the additional component of long-term social security benefits (the State Scheme). Other public sector schemes provide similar inflation-proofing, but rest on different legislation or agreements.

Membership

Brief notes on the members of the enquiry are attached. They are in no sense "representatives" but collectively offter great depth of experience and authority in a wide range of management and financial matters.

Cost

Global figures are not available (there are no central statistics of the costs of a large number of schemes under different managements). Figures of current and past pension payments can no doubt be obtained from individual managements (e.g. CSD for Civil Service and some other groups of employees). But to identify costs of 'index-linking' requires assumptions about an alternative basis with which to compare current and past costs, or a series of assumptions about future developments.

R. E. MACDONALD, M.A., F.F.A.

General Manager & Actuary and also Director
The Scottish Mutual Assurance Society

1942	M.A. (Hons. Mathematics and Natural Philosophy), Glasgow University.
1942-1946	War Service (Fl.Lt. R.A.F. (Signals)).
1950	Fellow of The Faculty of Actuaries.
1962-1969	Pensions Manager, The Scottish Mutual Assurance Society.
1969	General Manager & Actuary, The Scottish Mutual Assurance Society.
1976-1978	Chairman, Associated Scottish Life Offices.
1977-1979	President of The Faculty of Actuaries.

8th May, 1980

HAROLD B ROSE

H B Rose is Group Economic Adviser to Barclays Bank and Esmee Fairbairn Visiting Professor of Finance at the London Business School. He has recently served on the Research Panel of the Wilson Committee on the Functioning of Financial Institutions and is a Special Adviser to the Treasury and Civil Service Committee of the House of Commons.

Sir Alex Jarratt CB

Date of Birth	:	January 19th, 1924
Education	:	Royal Liberty Grammar School, Essex
University	:	Birmingham
Qualifications	:	Bachelor of Commerce (First Class Honours)
Decorations	:	Companion of the Order of the Bath, 1968. Knight Bachelor, 1979.
Honorary Degrees	:	Doctor of Science, Cranfield Institute of Technology, May 1973. Doctor of the University, Brunel University 1979
Family	:	Wife - Philomena. Three grown-up children: Helen, Ruth and Andrew
Address	:	Fryerning, Essex
Military Service	:	Fleet Air Arm

Career

1949	Ministry of Power - Assistant Principal. Promoted to Principal, 1953.
1954-55	Treasury
1955-59	Recalled to Ministry of Fuel and Power as Principal Private Secretary to Minister.
1959-63	Assistant Secretary, Ministry of Fuel and Power (Oil Division)
1963-64	Under-Secretary, Ministry of Fuel and Power (Gas Division).
1964-65	Under-Secretary Cabinet Office.
1965-68	First Secretary to the National Board for Prices and Incomes.
1968-70	Deputy Under-Secretary of State at the Department of Employment and Productivity.
1970 (June)	Deputy Secretary, Ministry of Agriculture.

1970	(Sept)	Resigned from Civil Service.
1970	(Oct)	Became Managing Director of IPC and was appointed to Boards of IPC and Reed International Limited.
1974	(Jan)	Appointed Chairman of IPC and IPC Newapapers (now known as Mirror Group Newspapers).
1974	(Dec)	Appointed Chairman & Chief Executive of Reed International Limited.

Non-Executive Directorships

Imperial Chemical Industries Limited

Midland Bank Limited

Supervisory Board of Thyssen-Bornemisza

Outside Activities

Chairman of Administrative Staff College, Henley

Governor of the London Business School

Governor of Ashridge Management College

Member of Court of Cranfield Institute of Technology

Member of the Council of the Industrial Society (Chairman 1975-79)

Member of the President's Committee of the Confederation of British Industry

Member of the National Economic Development Council

President of the Advertising Association

Vice-President of the Periodical Publishers Association Limited

April 1980

Personal: in confidence

Econ PS).

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

2nd May 1980

Sir Bernard Scott, KBE
C/o Miss Newland,
27, Berkeley Street,
LONDON. W1X 5HH

Dear Sir Bernard,

PENSIONS INQUIRY

You may find it helpful to have a progress report. There are also a few points on which we would be grateful for guidance.

First, membership. Sir Alex Jarratt, Professor Rose and Mr. Robert Macdonald, FFA, of the Scottish Mutual Assurance Society have agreed to serve as members. An invitation to serve on the Inquiry has been sent to Mr. Gavin Laird of the AUEW. If he is not prepared to take this on, Ministers have agreed that the Inquiry will proceed without a trade union member.

We have also arranged to provide you with a Secretary, Mr. P.J. (Peter) Farmer, a Principal who has been working in the Treasury recently, who will be available from 27th May to begin preparations, handle correspondence, etc., and who will look forward to meeting you as soon as you find it convenient thereafter. We shall also arrange for there to be a reference point in the Treasury to handle any written or telephone requests and representations. We must expect a great deal of public interest, and that many individuals and representatives of unions and other organisations will want to know about your arrangements to take evidence or want to seek an opportunity to put views to you.

I should be very grateful to know what line you would like us to take at this stage. It will of course be reasonable for you to defer decisions on what evidence you propose to take, from whom and in what form, and we could fend off

/enquiries

enquiries by saying simply that you and your colleagues will be considering how best to proceed and will make public your proposals later. We feel, however, that this might seem a little too negative. Hence the proposals incorporated in the attached documents for the announcement, in particular:-

- the sentence in the Parliamentary Answer: "I am sure it will want to consider representations both from those directly concerned and from others", which we think will give some reassurance;
- the address given in the draft press notice for any correspondence about the Inquiry;
- the paragraph in the background brief about 'representations'

We shall publish details of the Inquiry as soon as the question of Gavin Laird's membership is settled. Given the longish gap before the Inquiry starts it work, overshooting our self-imposed target of 30th April will do no harm.

Yours sincerely,

M A Hall

M.A. HALL
Private Secretary

Question: To ask the Prime Minister if she is satisfied that the value of index-linked pensions for public sector employees is adequately taken into account in contributions and levels of pay.

Draft Reply: Arrangements in different parts of the public sector vary widely and I am not satisfied that the difficult problem of the value of index-linked pensions has been adequately considered in all of them.

I am therefore setting up an independent enquiry to consider and advise on how such pensions might be valued. Sir Bernard Scott has agreed to be Chairman. Other members will be Sir Alex Jarratt, Professor Harold Rose, Mr Robert E. Macdonald, [Mr Gavin Lewis]

It is my hope that the enquiry can be completed within three or four months. I am sure it will want to consider representations both from those directly concerned and from others. It would then be for the Government and other public sector authorities to decide, in the light of the advice given, whether and what changes in present arrangements would be desirable. Any such changes would of course have to be considered by the managements and unions and staff associations concerned.

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/4.

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BACKGROUND BRIEF

General Comment

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For this reason, it should not be necessary for the enquiry to take extensive and detailed evidence in respect of the whole range of public sector pension schemes, which have many important differences of history, statutory or other basis, financial structure and details of calculation of benefits, and contributions.

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Representations

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/Details

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Membership

Brief notes on the members of the enquiry are attached. They are in no sense "representatives" but collectively offer great depth of experience and authority in a wide range of management and financial matters.

If asked why there is no trade union member, comment that there is no public service management member either: it should be emphasised that any future changes in existing public sector occupational pension arrangements will need to be fully discussed and negotiated between the managements and the unions and staff associations concerned.

Cost

Global figures are not available (there are no central statistics of the costs of a large number of schemes under different managements). Figures of current and past pension payments can no doubt be obtained from individual managements (e.g. CSD for Civil Service and some other groups of employees). But to identify costs of 'index-linking' requires assumptions about an alternative basis with which to compare current and past costs, or a series of assumptions about future developments.

- 6 MAY 1980

File

RH

APPOINTMENTS IN CONFIDENCE

Eca P31

30 April 1980

Pensions Enquiry

The Prime Minister has now read your letter of 25 April on the above subject. She has also seen your letter of 24 April to Richard Dykes and Andrew Hardman's reply of 28 April.

The Prime Minister is content for you to approach either Mr Bob Macdonald or Mr Ron Peat, or Mr R S Skerman. As for Trade Union representation, she believes Mr Gavin Laird would be a good choice if he were prepared to serve; but if not, she agrees with the Chancellor that the idea of a Trade Union member should be dropped.

I am sending copies of this letter to Andrew Hardman, (Department of Employment), Geoffrey Green (CSD) and David Wright (Cabinet Office).

T. P. LANKESTER

KRW

Martin A Hall, Esq MVO
HM Treasury

SW

APPOINTMENTS - IN CONFIDENCE

Econ Pol.

3pps

SECRETARY OF STATE FOR EMPLOYMENT

Caxton House Tothill Street London SW1H 9NA

Telephone Direct Line 01-213 6400

Switchboard 01-213 3000

M A Hall Esq
Private Secretary to the
Chancellor of the Exchequer
Treasury
Great George Street
LONDON SW1P 3AG

28/4

28 April 1980

Dear Martin,

PENSIONS ENQUIRY: TRADE UNION REPRESENTATION

You wrote to me on 24 April seeking views on the Chancellor's latest reflections.

My Secretary of State agrees that the inclusion of Frank Chapple would not carry much persuasive weight with other unions, and he shares the Prime Minister's doubts about the suitability of Geoffrey Drain for this particular enquiry. For his part he would have no objections to Gavin Laird of the AUEW, but doubts whether his inclusion would take any trick with those unions which have a major direct interest in the subject.

Reflecting on all of the difficulties my Secretary of State is, on balance, inclined to agree with the Chancellor that it might be better after all to do without a trade union member. We must expect some criticism, but it ought to be possible to limit this by careful presentation of the enquiry as a study by a team with relevant knowledge and experience whose report will be entirely open to discussion and, as appropriate, negotiations between the relevant managements and unions.

I am copying this letter to Tim Lankester.

Yours sincerely

ANDREW HARDMAN
Private Secretary

2 pps 1

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

25th April, 1980 Prime Minister

More difficulties in finalising membership of the pensions enquiry.

i) Are you content with these names as possibilities?

Yes.

ii) The Chancellor is now inclined – and Mr Prior agrees – to drop the idea of a trade union member (see Flag A). Are you content?

If necessary, but Gavin Laird is good.

TL.

28/4

T. Lankester, Esq.,
Private Secretary,
10, Downing Street

Dear Tim,

PENSIONS ENQUIRY

I am sorry to trouble you with a further letter about the membership of this group. The fact is, however, that Mr. R.E. Holland, after giving the invitation careful thought, has decided against acceptance. He felt that as an Actuary, even a non-practising one, he would find it difficult to avoid the appearance of being in professional dispute with the Government Actuary. I was unable to convince him that he would not be expected to make strictly Actuarial judgements, and that he was being invited as a prominent member of the insurance/pensions profession, rather than for his Actuarial qualifications. A second reason he gave for not wanting to accept the appointment was his feeling that this would be to some extent in conflict with his membership of the PRU.

Gordon Bailey has declined TL.

Apart from Gordon Bailey and Mr. Holland, the Chancellor's minute of 6th March to the Prime Minister mentioned two other possibilities, Bob Macdonald of the Scottish Provident, and Ron Peat, General Manager of Legal and General. A third possibility, recommended to me by Mr. Holland, is Mr. R.S. Skerman, CBE, who has just retired as Chief Actuary of the Prudential Assurance Company Limited.

I have not yet put Skerman's name to the Chancellor, who is abroad. But it would be helpful to have the Prime Minister's agreement to all these three names, so that (I hope!) we can avoid troubling you on this again.

I am copying this to Andrew Hardman, Geoffrey Green and David Wright.

Yours ever,

MAH

M.A. HALL
Private Secretary

A

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

24th April 1980

R. Dykes Esq.
Private Secretary to the
Secretary of State for Employment

Dear Richard,

PENSIONS ENQUIRY: TRADE UNION REPRESENTATION

As I mentioned to you on the telephone, the Chancellor has been having second thoughts about approaching Leif Mills. BIFU have, as you know, very recently been involved in the strike by Westminster Bank messengers, and difficult negotiations about the pay of other bank staff are now in prospect. The Chancellor thinks his inclusion would carry too high a risk of embarrassing the Government. He has considered various possible alternatives following discussion between Geoff Littler here and Douglas Smith in the DE.

The Chancellor does not favour an approach to David Lea, whom we identified in the earlier exercise as a second possibility. He feels that, however able, Lea is too much a part of the TUC establishment, and would feel obliged to act more as a representative of the TUC than as an independent member.

He then considered other possibilities, which can be summarised as follows:-

(i) Frank Chapple. The Chancellor recognises that he would be a co-operative member, if he agreed to serve, but doubts whether his membership would carry much weight in pursuading trade unions and their membership to accept the inquiry's conclusions, given his position on the spectrum of trade union opinion.

/(ii)

(ii) Gavin Laird. He was identified by officials as a rising and moderate trade union leader (he is a member of the Auew executive). He is not, however, known personally to the Chancellor.

(iii) Geoffrey Drain. The Chancellor would certainly not wish to press Drain's membership, and recognises the strength of the arguments the Prime Minister has put forward against it. He personally, however, would still see Drain as an outside possibility.

(iv) No trade union member at all.

With some reluctance, the Chancellor thinks that (iv) may be the most prudent course. We would be left with a sensible group of four with relevant experience and capacity for looking at a problem which does not split between management and unions, but rather between public and private sectors. If it were decided to drop a trade union member, however, we should need to look again at the presentation of the enquiry, to make it clear that any recommendations arising from it would, before being applied, naturally be a matter for negotiation between the relevant managements and unions.

The Chancellor would very much like to hear the views of the Secretary of State for Employment on this, before a final decision is taken.

I am copying this letter to Tim Lankester.

Yrs ever,

MH

M.A. HALL
Private Secretary

Econ P81

APPOINTMENTS IN CONFIDENCE

10 DOWNING STREET

From the Private Secretary

23 April 1980

Thank you for your letter of 21 April, about the team to conduct a business inquiry under Sir Bernard Scott's Chairmanship.

I confirm that the Prime Minister is content that Mr. Holland should now be approached.

I am sending copies of this letter to Andrew Hardman (Department of Employment), Geoffrey Green (CSD) and David Wright (Cabinet Office).

M. A. PATTISON

Martin Hall, Esq., MVO,
H.M. Treasury.

TLR

APPOINTMENTS IN CONFIDENCE

1.

PRIME MINISTER

Mr Bailey is not available for the pensions enquiry. Agree Mr R E Holland of Pearl Assurance instead?

MAP 22/4

Yes MT

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

M Patterson Esq
No 10 Downing Street
London SW1

21 April 1980

Dear Mike,

PENSIONS INQUIRY

John Wiggins wrote to Tim Lankester on 11 April giving a final list of people we intended to approach with invitations to serve on the proposed independent inquiry under Sir Bernard Scott's Chairmanship. So far, Alex Jarratt and Harold Rose have agreed to serve. Gordon Bailey, however, has reluctantly declined, on the (understandable) grounds that the Wilson Committee proved to be a very much larger investment in time than he had expected, and that his Company and family commitments must now take precedence. Our second name in the insurance field was Mr R E Holland, Chief General Manager of Pearl (see Annex A of the Chancellor's minute of 6 March). I should be grateful for your confirmation that the Prime Minister is content that I should now approach Mr Holland.

We have not yet written to Leif Mills.

I am copying this letter to Andrew Hardman, Geoffrey Green and David Wright.

Yours ever,

MAH

M A HALL
Private Secretary

SECRET

Econ Pol.

cc: Master Set
Iran Sit
Nat Ind - Public Pay
Aug 79

10 DOWNING STREET

From the Principal Private Secretary

17 April 1980

When the Chancellor of the Exchequer called upon the Prime Minister at 0900 this morning the following were the main points which arose in discussion.

IRAN

The Chancellor of the Exchequer said that he had let the Governor of the Bank of England know the conclusions which OD had reached at its meeting on 15 April. The Governor was very concerned that there should be no discussion at the forthcoming meeting of the Foreign Affairs Council of the possibility of taking legislation to provide for mandatory action on Iranian loans, deposits and credits.

The Prime Minister said that OD had agreed that it would be preferable to take action on this point by means of persuasion rather than by legislation. The Chancellor should minute other members of OD explaining the Governor's concern and asking for their agreement that the Foreign and Commonwealth Secretary should not mention the possibility of legislation for this purpose at next week's meeting with the other Foreign Ministers of the Nine.

PUBLIC SECTOR PENSIONS

The Prime Minister said that she remained of the view that Mr. Drain should not be invited to become a member of Sir Bernard Scott's group on index linked pensions in the public sector. Mr. Drain was the leader of a union whose members now enjoyed inflation proof pensions and as such he would find it impossible to make a proper contribution to the enquiry.

The Chancellor of the Exchequer said that he would arrange for Mr. Leif Mills to be invited instead.

PUBLIC SECTOR PAY

The Chancellor said that he hoped to bring forward quickly the work which he already had in hand on public sector pay. In the meantime it was important to correct the wrong impressions which had resulted from his appearance before the Select Committee on the Treasury and Civil Service earlier in the week. There was now a belief

/that the

SECRET

E.R.

SECRET

that the going rate for public sector pay in the present year was 25%. He was proposing to issue a statement either today or tomorrow which would make clear that the figures which he had quoted to the Select Committee embraced a good deal of catching up pay awards of the Clegg kind and that they were fully consistent with approved cash limits.

More generally, the future level of pay settlements was critical to the attempt to reduce the money supply. It looked as though the money supply figures for this month would come out satisfactorily, though inter bank lending was still running at too high a level. The new tap stock looked as though it would go well. But the fact was that because pay settlements were still at very high levels, they were putting up borrowing and helping to keep up interest rates.

The Prime Minister said that she would consider including something about the level of public sector pay increases in the speech she was due to give in Birmingham on Monday of next week. Looking further ahead to the next pay round, she believed that it was important to have an assessment of our ability to withstand a national rail strike. This meant essentially forming a view on whether the power stations could keep going during such a strike. She proposed to have a meeting with the Home Secretary, the Chancellor, the Secretary of State for Energy and the Minister of Transport to consider what work needed to be set in hand on this.

SELECT COMMITTEE ON THE TREASURY AND CIVIL SERVICE

The Chancellor said that his appearance before the Select Committee had shown that its members were determined, regardless of Party, to attack the Government wherever they could. Mr. du Cann wanted to maintain the unity of his Committee and not to let it divide on Party lines. The Chancellor added that he was due to appear before the Select Committee again in the near future and he expected that one of the principal areas of questioning would be unemployment. The Committee would be bound to press him for the Government's assumptions and predictions for future trends in unemployment, but he proposed to tell them that there were many areas where the Government could not hazard forecasts.

C. A. WHITMORE

cc J. Hoskyns

A.J. Wiggins, Esq.,
HM Treasury.

SECRET

GB

CONFIDENTIAL

10

MAP 17/4.

cc - ~~Mr Lankester - No 10~~
Mr G E T Green
Mr Laughrin
Mr Priestley -
Cabinet Office

Mr Gaffin
No 10

Top copy on
Govt Machinery Pt 5
Efficiency & Waste.

EFFICIENCY: PUBLICITY

Mr Priestley kindly copied to me his minute of 10 April.

You and I will certainly need to keep in touch about publicity for any Cabinet decisions on manpower and efficiency which are made in the near future. My Minister of State envisages that any decisions would be announced more or less immediately they are taken, and we are assuming here that it is likely to be CSD who will be making the announcement.

We also need to keep in touch about what line should be taken with the press if the fact that there is to be a Cabinet meeting on this subject leaks out.

Following the article in this week's Sunday Telegraph, the CSD is dealing appropriately with the National Staff Side.

Perhaps I may take this opportunity of commenting on Mr Desmond Quigley's request for an interview with Sir Derek Rayner. Sir Derek will of course have his own views about this, but Mr Priestley may like to know that "Financial Weekly" have recently made a conscious decision (we have been explicitly told this) to change their previous policy of giving reasonably fair treatment to Civil Service affairs to one of hostility to the Service. This is illustrated by the attached cutting from the edition of 4 April, with its wholly unfounded attack on Sir Ian Bancroft and Sir John Herbecq, which was largely the work of Mr Quigley. As far as the CSD is concerned, therefore, Mr Quigley does not now rate highly on our list of people to whom we are willing to give facilities.

JSB

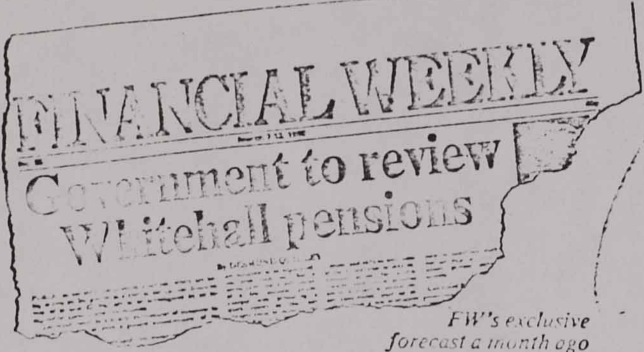
J S Beastall
Information Services

16 April 1980

ENC

CONFIDENTIAL

Financial Weekly
4/4/80


FINANCIAL WEEKLY

Government to review Whitehall pensions

FW's exclusive forecast a month ago

Whitehall beats its mistress

WOULD SIR Ian Bancroft and Sir John Herbecq please come forward and take a bow before their 7.2m fans?

Sir Ian, Permanent Secretary at the Civil Service Department and Head of the Home Civil Service, and his No 2 Sir John, who are both 57, have managed to frustrate the pension desires of the Prime Minister.

Margaret Thatcher wanted to abolish public sector index-linked pensions. So did Chancellor Sir Geoffrey Howe and a few other Cabinet colleagues. But Bancroft and Herbecq were not happy with the idea, nor were some other Cabinet members. Other Ministers were on the sidelines until the Bancroft/Herbecq team got to work.

Bancroft and Herbecq, of course, know what they are talking about. In their time they have both headed the Civil Service superannuation division. And Herbecq was the architect of the Pensions (Increase) Act 1971 which put index linking for civil servants on a permanent basis. So who better to tell their peers in other Departments the advice to be given to their Ministers sitting on Cabinet Committee E — the committee dealing with the pensions question.

The upshot was that Defence Secretary Francis Pym, whose Permanent Secretary, Sir Frank Cooper, is a real Whitehall heavyweight, and Home Secretary Willie Whitelaw sided with the well-known wets on Committee E and watered down the already weak Cabinet decision on an inquiry.

Having lost the Cabinet battle to scrap index-linked pensions, Thatcher is now faced with an inquiry — forecast exclusively in *Financial Weekly* a month ago, and announced by Howe in his Budget — which has had its teeth drawn even before it starts, through circumscribed terms of reference.

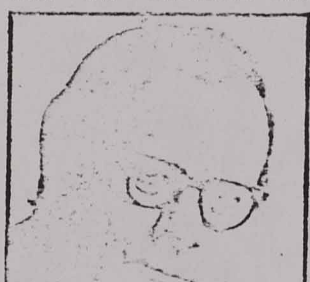
Instead of fundamentally questioning whether it is equitable that one section of the community should have the privilege of index-linking while the rest does not, the inquiry will be required only to consider what should be the cost to public servants of having their inflation proofing, a figure which has anyway been produced for years by the Government Actuary and which is actually garbage. (The private pensions industry says it is actuarily impossible to produce a correctly funded inflation-proof scheme.)

So Bancroft and Herbecq have saved the current 4.9m public service workers and the 2.3m public service pensioners from having their pension arrangements being messed around. The 2.3m pensioners — who include ex-MPs, civil servants, gasmen, postmen and local authority workers — are costing £2.9bn to keep index-linked this year.

Meanwhile the hunt for the chairman of the five-man inquiry goes on.

Those on the Civil Service Department's list of the "Great and the Good" are proving remarkably reluctant to take on the job.


SIR JOHN HERBECQ


SIR IAN BANCROFT

PRIME MINISTER

Meeting with the Chancellor of the Exchequer
at 0900 Thursday, 17 April 1980

I am not aware of any specific subjects which you need to raise with the Chancellor of the Exchequer when you see him at 0900 tomorrow morning.

The only item he is likely to bring up is the question of appointing a trade unionist as a member of Sir Bernard Scott's group on index linked pensions. You will remember that you remain unhappy about the proposal to invite Mr. Geoffrey Drain to join the group. I attach the most recent papers on this.

It is also possible that the Chancellor will want a general word with you about our contribution to the Community Budget and the run up to the meeting of the European Council.

[illegible]

16 April 1980

[illegible]

APPOINTMENTS IN CONFIDENCE

File B

Econ Pol.

10 DOWNING STREET

From the Private Secretary 15 April 1980

We spoke yesterday about the composition of Sir Bernard Scott's pensions enquiry team, about which you wrote to Tim Lankester on 11 April.

The Prime Minister has taken another look at the proposal to approach Geoffrey Drain as the first preference for the fourth slot. She is, however, still of the view that it would be a mistake to make the trade unionist the one member of the team linked to inflation-proofed pension interests. As I told you yesterday, she is also concerned about the risk of stimulating a minority report in this way.

I am sending copies of this letter to David Edmonds (Department of the Environment), Andrew Hardman (Department of Employment), Geoffrey Green (Civil Service Department) and David Wright (Cabinet Office).

M. A. PATTISON

A.J. Wiggins, Esq.,
H.M. Treasury.

1

PRIME MINISTER

You queried Geoffrey Drain, on the basis that this is a recipe for a minority report.

Sir Bernard Scott is essentially arguing that his Group's credibility will be much strengthened by having a representative of some of the staff who benefit from inflation-proofed pensions. He recognises the risk, but argues that it is worth taking for the chance of producing a report carrying some real weight. The Chancellor accepts Sir Bernard's view, and he feels that Drain is a sufficiently independent character to bring some objectivity to the task.

Would you still prefer to avoid bringing in a fourth member of the team who comes from the "inflation-proofed" camp?

14 April 1980

I think it a mistake to make the <u>T.U. nominee</u> the representative of inf-proofed pensions

MT

1

APPOINTMENTS - IN CONFIDENCE

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

11th April 1980

T.P. Lankester Esq.
No. 10 Downing Street
London
SW1

Prime Minister

Agree that the Chancellor should approach Geoffrey Drain for the trade union member?

TL 11/4

But Drain's people receive inflation proof pensions in full so we shall be heading for a priority report. MT

Dear Tim,

PENSIONS ENQUIRY

We have now had comments from Sir Bernard Scott on the suggested members of the team under his Chairmanship. Subject to one point which the Chancellor would like you to mention to the Prime Minister, I think we are clear to go ahead and try to recruit.

As regards three of the four names, Sir Bernard Scott's thoughts fit what we had in mind:

- Gordon Bailey as somebody experienced in the Insurance Industry.
- Alex Jarratt or Alan Lord (in that order of preference) as a candidate with mixed public sector and industry experience.
- Harold Rose or Andrew Bain as an economist (in that order in the light of Scott's very high opinion of Harold Rose). The only possible impediment if that Rose is known as an occasional adviser to the Industry Secretary and has recently been included in the list of advisers recruited by the Treasury and Civil Service Committee of the House of Commons. If selected for the pensions enquiry, he might feel that he must let these other functions lapse for a period, but we do not think they constitute an objection to choosing him.

/The remaining

The remaining post is the one for which we need a trade unionist, and you will remember that we had in mind either Leif Mills or David Lea. Without rejecting these names, Scott has suggested that there would be advantage in having somebody more "operational" who would carry authority among public sector employees, and he has very strongly recommended Geoffrey Drain of NALGO, with David Basnett of GMWU as a possible alternative. On reflection, and having a good opinion of Drain's ability and constructiveness, the Chancellor is inclined to support Scott's proposal. There can be no doubt that a satisfactory recommendation carrying Drain's support would be helpful as far as public sector unions were concerned. Given the balance of membership as a whole, the Chancellor does not feel that the inclusion of Drain would lead to any accusations of bias.

Perhaps you could let me know whether the Prime Minister would be content to try Drain in preference to the other names we had previously agreed. I am also copying this letter to David Edmonds (Environment), Andrew Hardman (Employment) and Geoffrey Green (CSD), in case their Ministers have any quick comments, and to David Wright (Cabinet Office).

Yours

John

A.J. WIGGINS
Private Secretary

11 APR 1980

PT

CONFIDENTIAL

Econ. Pol 1

DEPARTMENT OF EDUCATION AND SCIENCE

ELIZABETH HOUSE,
YORK ROAD,
LONDON SE1 7PH
01-928 9222

FROM THE SECRETARY OF STATE

M A Hall Esq
Private Secretary to the
  Chancellor of the Exchequer
Treasury Chambers
Parliament Street
LONDON SW1

10 April 1980

Dear Martin,

INDEPENDENT INQUIRY INTO THE VALUE OF PENSIONS

We have only one comment of substance on the set of drafts you sent Tim Lankester on 1 April.

The sixth line of paragraph 3 of the notes for editors speaks of "an appropriate level of employee contributions". As there can presumably be no reason for pre-judging that any change that the Inquiry thought appropriate should apply only to employees' and not to employers' contributions, it might be better to delete the word "employee".

We expect you have already deleted "today" from the opening sentence of the notes for editors. And in the third line of the third sub-paragraph of the background brief, accuracy requires "....teachers and other local authority....."

I am copying this letter to the recipients of yours.

Yours faithfully

Pete

P A SHAW
Private Secretary

CONFIDENTIAL

TPL(OR)

mjs 9/4

MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1
Telephone 01-~~XXX XXXX~~ 218 2111/3

SECRETARY OF STATE

MO 20/17/6

8th April 1980

10/4

Dear Martin,

Thank you for letting us see the drafts you sent to Tim Lankester concerning the independent enquiry into the value of public sector pensions. The Ministry of Defence has two comments - both relatively minor - which may already have been made by others.

Paragraph 3 of the draft press notice refers to "an appropriate level of employee contributions". As Civil Service, and, I believe, other public sector, pensions are non-contributory, it might be helpful to press home the point that both contributory and non-contributory schemes are being reviewed. This might be done conveniently by adding a passage such as: "....... or reflected at an appropriate level in the settlement of pay".

The drafts do not refer to consultation with the representatives of the public sector employees concerned and, indeed, decisions may not have been taken on how this would be done. Assuming, however, that there will be such discussion at a suitable point, it might be helpful presentationally to touch on this. It could be done by expanding the final sentence of the second paragraph of the Prime Minister's reply to read: "....... of the advice given and after appropriate consultation, whether and how ....".

I have copied this to Tim Lankester (No 10), Geoffrey Green (CSD), and David Wright (Cabinet Office).

Yours ever

David Omand

(D B OMAND)
Private Secretary

cc Cabinet
CSD
CO

Econ Pol.

10 DOWNING STREET

From the Private Secretary

8 April 1980

Independent Inquiry into the Value on Pensions

The Prime Minister has now considered your letter of 1 April and the draft Terms of Reference, etc., which you enclosed with it. She has asked me to say that she is content with these drafts.

I am sending copies of this letter to the Private Secretaries to the members of the Cabinet, to Geoffrey Green (Civil Service Department) and David Wright (Cabinet Office).

T. P. LANKESTER

M. A. Hall, Esq., M.V.O.,
H.M. Treasury.

FILE

CONFIDENTIAL

RH

cc Press Office

10 DOWNING STREET

From the Private Secretary

3 April 1980

The Chancellor had a word with the Prime Minister this morning about the Chairmanship of the proposed enquiry into the value of indexed linked pensions. He told the Prime Minister that, as she had agreed, he had approached Sir Bernard Scott to see if he would be willing to take on the Chairmanship. Sir Bernard had said that he would, but would only be able to start work in July. The Chancellor's inclination was to confirm the appointment on those terms - since it would be difficult to find a suitable alternative name, and the Committee would still be able to complete its work in plenty of time before next year's Civil Service pay negotiations.

The Prime Minister said that she was content for the Chancellor to proceed on this basis. He should confirm Sir Bernard's appointment with him and consult with him on the other members of the Committee with a view to an announcement, if possible, by the end of April.

T. P. LANKESTER

Martin A Hall, Esq MVO
HM Treasury

KRB

CONFIDENTIAL

CHANCELLOR OF THE EXCHEQUER

With the Compliments
of the
Chancellor of the Exchequer's
Private Secretary

Treasury Chambers,
Parliament Street,
S.W.1.

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

3rd April, 1980

R.
8/4

Sir Bernard Scott, Kt., CBE., TD.,
Lucas Industries Limited,
46, Park Street,
LONDON,
W.1.

Dear Sir Bernard,

INDEPENDENT INQUIRY INTO THE VALUE OF PUBLIC SERVICE INDEX LINKED PENSIONS

I am writing to follow up your discussion this morning with the Chancellor of the Exchequer. Sir Geoffrey was very grateful for your agreement to take up the Chairmanship of the Independent Inquiry outlined in his Budget Speech, but felt that he should consult the Prime Minister given that you will not be available until the end of June or the beginning of July. I can now confirm that the Prime Minister has approved the appointment, on the basis that you will start then. The Prime Minister and the Chancellor do however very much hope that you will be able to find some little time between your return to this country and your stay in hospital to discuss further the programme and working methods of the Inquiry. No doubt we can make arrangements through your office in London.

.... The Government proposes to announce the establishment of the Inquiry along the lines of the enclosed Parliamentary Question & press notice. Announcement will be deferred until the membership of the Inquiry has been established; but the Government's strong hope is that this can be done before the end of this month. Also enclosed are the proposed terms of reference of the Inquiry.

The Chancellor promised to consult you about membership. We have not yet approached anyone, but the names which Ministers favour are as follows.

On the trade union side, the two front runners have been Leif Mills and David Lea. On balance, the Chancellor is inclined towards Mills, and you were of the same view. It was thought helpful to have someone from the insurance

/industry

industry, and here the preferred candidate is Gordon Bailey, of the National Provident, a past president of the Institute of Actuaries, and a member of the Wilson Committee. Among professional economists, Andrew Bain of Edinburgh University is the preferred choice, though Harold Rose is another possibility. There are several possibile candidates with mixed public and private sector experience. Here, Ministers' preference is for Alan Lord, though Alex Jarratt would be another strong possibility. I should emphasise that although Ministers have already given a good deal of thought to membership, the options are not necessarily closed off by this list of names, and your own suggestions would be very welcome.

I look forward to hearing from you.

With many thanks again on the Chancellor's behalf, and best wishes for a very successful farewell tour.

Yours sincerely,

M A Hall

M.A. HALL
Private Secretary

Question: To ask the Prime Minister if she is satisfied that the value of index-linked pensions for public sector employees is adequately taken into account in contributions and levels of pay.

Draft Reply: Arrangements in different parts of the public sector vary widely and I am not satisfied that the difficult problem of the value of index-linked pensions has been adequately considered in all of them.

I am therefore setting up an independent enquiry to consider and advise on how such pensions might be valued. [.................. has agreed to be Chairman. Names of other members of the enquiry team will be announced later. It is my hope that the enquiry can be completed within three or four months. It would then be for the Government and other public sector authorities to decide, in the light of the advice given, whether and how changes in present arrangements should be made.

The full terms of reference will be as follows:

[Take in text of terms of reference].

TERMS OF REFERENCE

Having regard to the need to ensure that full account is taken in all areas of the public sector, whether by contributions or salary abatement, of the value of inflation-proofing of occupational pensions, and of relative job security, taking due account of arrangements in the private sector:

(a) to consider the assumptions and methods used by the Government Actuary where he assesses the value of differences in inflation-proofing;

(b) to consider the relative degree of security in the full inflation-proofing enjoyed by public sector employees compared with those in the private sector, and the additional value to be placed upon it;

(c) to consider how to assess the relative job security enjoyed by employees in the private and public sectors;

(d) to report their conclusions and suggest what valuations or methods of valuation would be appropriate to take account of them in determining pay and other conditions of service.

DRAFT PRESS NOTICE

ENQUIRY INTO VALUE OF PENSIONS

The Prime Minister gave the following reply today to a Parliamentary Question about the value of index-linked pensions for public sector employees:

"[Take in text of reply]".

NOTES FOR EDITORS

This is the enquiry which was also mentioned in the Chancellor's Budget Speech ~~today~~.

2. The Government is concerned about the arrangements for index-linked occupational pensions almost throughout the public sector, which are not matched by occupational pensions in the private sector. The difference of pension treatment and its cost have become important as a result of several years of high rates of inflation, and has attracted strong criticism. The Government is dedicated to the objective of reducing inflation, and success in that will diminish the problems arising from different kinds of pension treatment. Nevertheless, those problems do at present exist, and need urgent consideration.

3. Pension schemes and the benefits attached to them involve long-run expectations and commitments which should not lightly be interfered with. The Government is conscious of the obligations it has inherited towards its own direct employees and other employees in the public sector. Nevertheless, any Government must ultimately reserve the right to reconsider the arrangements for full inflation-proofing of public sector occupational pensions against the background of national economic and social considerations.

/4.

4. First, however, the Government wishes to explore more thoroughly the question whether the additional advantages of index-linked pensions can be adequately valued, and their additional value translated into an appropriate level of employee contributions. The purpose of the proposed enquiry is to seek advice on the problem of valuation. It would then be for the Government and other public sector authorities to decide, in the light of the advice given, whether and how changes in present arrangements should be made.

5. The terms of reference specify two particular elements in valuation which seem to be worth attention: first, one which arises only where (as in the case of the non-industrial Civil Service and some other public sector groups) a deliberate attempt is made to cost the effect of inflation-proofing for future years; the other an attempt to get at the elusive problem of valuing security in an uncertain world.

6. The terms of reference also refer to the problem of relative job security. This is of course separate from the pensions valuation problem, but could involve some similar considerations. It has been included in the hope that the enquiry might, in the course of considering security of pensions value, develop ideas which could help in considering job security also.

BACKGROUND BRIEF

Membership

A further announcement will be made when the team for the proposed enquiry has been completed. It is envisaged that the team will consist of some four people in addition to the Chairman, representing a range of experience.

Representations

The Chairman of the Enquiry will no doubt publicise soon his proposals to receive any representations. Meanwhile any comments addressed to "Enquiry into Value of Pensions", c/o H.M. Treasury, Parliament Street, London, SW1P 3AG, will be acknowledged and forwarded to the Chairman.

What Public Sector Pension Schemes are Index-Linked?

Nearly all, which makes a very long list, including Civil Service, Ministers, Members of Parliament, Judiciary, Armed Forces, Police, Nurses, Doctors, Teachers, and local authority and nationalised industry employees. In total, some 5½ million present employees in the public sector are covered by index-linked pension schemes.

Details of Schemes

Details vary, and enquiries should be referred to the managements of the particular public sector groups concerned.

Basis of Present Index-Linking

A large collection of "official pensions", mainly but not exclusively central and local government employees, are covered by the 1971 Pensions (Increase) Act, read in conjunction with other pensions legislation, notably the Social Security Pensions Act 1975. Official pensions are increased in line with forecast movements of the retail price index, at the same time and by the same amount as the additional component of long-term social security benefits (the State Scheme). Other public sector schemes provide similar inflation-proofing, but rest on different legislation or agreements.

Cost

Global figures are not available (there are no central statistics of the costs of a large number of schemes under different managements). Figures of current and past pension payments can no doubt be obtained from individual managements (e.g. CSD for Civil Service and some other groups of employees). But to identify costs of "index-linking" requires assumptions about an alternative basis with which to compare current and past costs, or a series of assumptions about future developments.

General Comment

It is important to emphasise that the enquiry is addressed to the important general issue of valuation. It is not being asked to examine in detail the precise arrangements and commitments of existing pension schemes, far less to set out any blue-print of how such schemes might be changed.

For this reason, it should not be necessary for the enquiry to take extensive and detailed evidence in respect of the whole range of public sector pension schemes, which have many important differences of history, statutory or other basis, financial structure and details of calculation of benefits, and contributions.

Confidential

Prime Minister

Content?

TL 3/4

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

T Lankester Esq
No 10 Downing Street
London SW1

1 April 1980

We discussed this with C-of-E and decided to hold the announcement until we have for the names of all the members of the enquiry. Otherwise agreed

Dear Tim

INDEPENDENT INQUIRY INTO THE VALUE OF PENSIONS

In my letter to you of 25 March reporting that we had not yet found a Chairman for the Inquiry and would therefore be deferring the formal announcement, I mentioned that this would give us time to settle one or two drafting points on the Press Notice, Background Briefing, etc.

I now enclose a slightly revised set of papers, consisting of:

- Draft for an arranged Question and Answer by the Prime Minister;
- Draft Terms of Reference;
- Draft Press Notice and Notes for Editors;
- Draft Background Briefing;

The amendments incorporated in these slightly revised drafts reflect one or two second thoughts and comments by particular Ministers. Perhaps the most important comment made, by both the Transport Minister and the Minister of State for the Civil Service, was that they did not like the sentence in paragraph 3 of the Notes for Editors which pointed to the possibility of future Government consideration of the basic index-linking arrangements. This is met to the extent of removing the point from the Notes for Editors - now much shorter in any case - but retaining it in background briefing for answering questions. I hope this will be acceptable.

I am copying this letter and the enclosures to the Private Secretaries to other members of the Cabinet, to Geoffrey Green and to David Wright. I would be grateful if any further comments which their Ministers wish to make could be conveyed to me by close of play on Wednesday 9 April.

You told the Chancellor to announce when he has all the members lined up.
TL.

Yours ever,

M A HALL
Private Secretary

Question: To ask the Prime Minister if she is satisfied that the value of index-linked pensions for public sector employees is adequately taken into account in contributions and levels of pay.

Draft Reply: Arrangements in different parts of the public sector vary widely and I am not satisfied that the difficult problem of the value of index-linked pensions has been adequately considered in all of them.

I am therefore setting up an independent enquiry to consider and advise on how such pensions might be valued. [.................] has agreed to be Chairman. Names of other members of the enquiry team will be announced later. It is my hope that the enquiry can be completed within three or four months. It would then be for the Government and other public sector authorities to decide, in the light of the advice given, whether and how changes in present arrangements should be made.

The full terms of reference will be as follows:

[Take in text of terms of reference].

TERMS OF REFERENCE

Having regard to the need to ensure that full account is taken in all areas of the public sector, whether by contributions or salary abatement, of the value of inflation-proofing of occupational pensions, and of relative job security, taking due account of arrangements in the private sector:

(a) to consider the assumptions and methods used by the Government Actuary where he assesses the value of differences in inflation-proofing;

(b) to consider the relative degree of security in the full inflation-proofing enjoyed by public sector employees compared with those in the private sector, and the additional value to be placed upon it;

(c) to consider how to assess the relative job security enjoyed by employees in the private and public sectors;

(d) to report their conclusions and suggest what valuations or methods of valuation would be appropriate to take account of them in determining pay and other conditions of service.

DRAFT PRESS NOTICE

ENQUIRY INTO VALUE OF PENSIONS

The Prime Minister gave the following reply today to a Parliamentary Question about the value of index-linked pensions for public sector employees:

"[Take in text of reply]".

NOTES FOR EDITORS

This is the enquiry which was also mentioned in the Chancellor's Budget Speech today.

2. The Government is concerned about the arrangements for index-linked occupational pensions almost throughout the public sector, which are not matched by occupational pensions in the private sector. The difference of pension treatment and its cost has become important as a result of several years of high rates of inflation, and has attracted strong criticism. The Government is dedicated to the objective of reducing inflation, and success in that will diminish the problems arising from different kinds of pension treatment.

3. But widespread doubts have been expressed about the valuation of the benefit of index-linking and the Government wishes to explore thoroughly the question whether the additional advantages of index-linked pensions can be adequately valued, and their additional value translated into an appropriate level of employee contributions. The purpose of the proposed enquiry is to seek advice on the problem of valuation. It would then be for the Government and other public sector authorities to decide, in the light of the advice given, whether and how changes in present arrangements should be made.

4. The terms of reference specify two particular elements in valuation which seem to be worth attention: first, one which arises only where (as in the case of the non-industrial Civil Service and some other public sector groups) a

/deliberate

deliberate attempt is made to cost the effect of inflation-proofing for future years; the other an attempt to get at the elusive problem of valuing security in an uncertain world.

5. The terms of reference also refer to the problem of relative job security. This is of course separate from the pensions valuation problem, but could involve some similar considerations. It has been included in the hope that the enquiry might, in the course of considering security of pensions value, develop ideas which could help in considering job security also.

BACKGROUND BRIEF

Membership

A further announcement will be made when the team for the proposed enquiry has been completed. It is envisaged that the team will consist of some four people in addition to the Chairman, representing a range of experience.

Representations

The Chairman of the Enquiry will no doubt publicise soon his proposals to receive any representations. Meanwhile any comments addressed to "Enquiry into Value of Pensions", c/o H.M. Treasury, Parliament Street, London, SW1P 3AG, will be acknowledged and forwarded to the Chairman.

What Public Sector Pension Schemes are Index-Linked?

Nearly all, which makes a very long list, including Civil Service, Ministers, Members of Parliament, Judiciary, Armed Forces, Police, Nurses, Doctors, Teachers, and local authority and nationalised industry employees. In total, some 5½ million present employees in the public sector are covered by index-linked pension schemes.

Details of Schemes

Details vary, and enquiries should be referred to the managements of the particular public sector groups concerned.

Basis of Present Index-Linking

A large collection of "official pensions", mainly but not exclusively central and local government employees, are covered by the 1971 Pensions (Increase) Act, read in conjunction with other pensions legislation, notably the Social Security Pensions Act 1975. Official pensions are increased in line with forecast movements of the retail price index, at the same time and by the same amount as the additional component of long-term social security benefits (the State Scheme). Other public sector schemes provide similar inflation-proofing, but rest on different legislation or agreements.

Cost

Global figures are not available (there are no central statistics of the costs of a large number of schemes under different managements). Figures of current and past pension payments can no doubt be obtained from individual managements (eg CSD for Civil Service and some other groups of employees). But to identify costs of 'index-linking' requires assumptions about an alternative basis with which to compare current and past costs, or a series of assumptions about future developments.

General Comment

It is important to emphasise that the enquiry is addressed to the important general issue of valuation. It is not being asked to examine in detail the precise arrangements and commitments of existing pension schemes, far less to set out any blue-print of how such schemes might be changed.

For this reason, it should not be necessary for the enquiry to take extensive and detailed evidence in respect of the whole range of public sector pension schemes, which have many important differences of history, statutory or other basis, financial structure and details of calculation of benefits, and contributions.

Continuation of Index-Linking

The enquiry is concerned with the valuation of index-linking, not with the appropriateness of index-linking itself. Pension schemes and the benefits attached to them involve long-run expectations and commitments which should not lightly be interfered with. The Government is conscious of the obligations it has inherited towards its own direct employees and other employees in the public sector. Nevertheless, any Government must ultimately reserve the right to reconsider the arrangements for full inflation-proofing of public sector occupational pensions againstthe background of national economic and social considerations.

2 - APR 1980

CONFIDENTIAL

file D G

Econ Pol.

10 DOWNING STREET

From the Principal Private Secretary

1 April 1980

Dear John,

INDEPENDENT INQUIRY INTO THE VALUE OF PENSIONS

The Prime Minister and the Chancellor of the Exchequer had a further word this morning about possible candidates to chair this proposed Inquiry. The Prime Minister agreed that the Chancellor should approach Sir Bernard Scott who is to retire shortly from his present post as Chairman of Lucas.

I am sending copies of this letter to the Private Secretaries to other members of the Cabinet, Geoffrey Green (CSD) and to David Wright (Cabinet Office).

Yours ever,

Clive Whitmore.

John Wiggins, Esq.,
H. M. Treasury.

CONFIDENTIAL

CONFIDENTIAL

Prime Minister

1

cc. Mr Ingham.

MB.

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

T Lankester Esq
Private Secretary to the
Prime Minister
No 10 Downing Street

25 March 1980

Dear Tim,

INDEPENDENT INQUIRY INTO THE VALUE OF PENSIONS

As you know, we have not yet managed to obtain the services of a suitable independent Chairman for this proposed inquiry. I reported yesterday that neither Sir Rowland Wright nor Sir Alastair Pilkington felt they could spare the time to do justice to the job.

In these circumstances, the Chancellor thinks it would be a mistake to make a formal announcement about the inquiry, and has therefore dropped the idea of issuing a press notice and tabling an arranged PQ tomorrow. He will, however make a brief allusion to the problem during his Budget Speech, and will state the Government's intention of setting up an inquiry. As soon as the Budget is out of the way, we shall need to revert to the question of the chairmanship, before assembling a team and making the detailed announcement as soon as possible. This would incidentally also give a little more time in which to settle one or two late comments from other Ministers about the draft press notice and the background briefing.

I am copying this letter to the Private Secretaries to other members of the Cabinet, to Geoffrey Green, and to David Wright.

Yours ever,

M A HALL
Private Secretary

Prime Minister.

The Chancellor is not too keen on the other two names we suggested. Cadbury is felt to be too closely identified with the CBI; and Fraser is said to be 'past it'!

TPL
25.iii

– But he's a comparatively young man!

MT

Clive

Chancellor will come back on Scott at tomorrow's breakfast. (It would be very good if he could announce the inquiry in his Budget wind-up after the criticism that he is vacillating on this issue.)

T.

31/3

PRIME MINISTER

The Inquiry into Civil Service Pensions

Rowland Wright has turned down the Chairmanship of the pension inquiry. As you know, the Chancellor intends to announce the inquiry in his Budget speech, and therefore ideally we would like to have at least a chairman by then. He would now like to approach Bernard Scott, the Chairman of Lucas. He is retiring shortly, and could well be available to take this on. Would you be content?

T.

24 March 1980

Tim

The Prime Minister is not happy with Scott. She prefers:-

1. Alastair Pilkington
2. Adrian Cadbury
3. Campbell Fraser

in that order.

AHW 24/iii

with compliments

MINISTER OF STATE

CIVIL SERVICE DEPARTMENT
Whitehall London SW1A 2AZ

Telephone 01-273 5563/4086

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Civil Service Department
Whitehall London SW1A 2AZ
Telephone 01-273 3000

Minister of State

M A Hall Esq MVO
Private Secretary
Chancellor of the Exchequer
HM Treasury
Treasury Chambers
Parliament Street
LONDON SW1P 3AG

R 24/3

24 March 1980

Dear Martin,

INDEX-LINKED OCCUPATIONAL PENSIONS

The Minister of State has asked me to let you have comments on the draft Press Notice and briefing attached to your letter of 20 March to Tim Lankester at No 10.

2. The Minister of State would like to see an amendment to the third sentence in paragraph 3 of the draft Notes to Editors. He believes that if this sentence was repeated by the Press, it would acutely alarm large numbers of public service pensioners, while doing nothing to convince private sector critics of the existing arrangements. We would suggest as an alternative:

> "It believes, however, that where full inflation-proofing is provided, public servants should pay a fair contribution towards the cost, taking into account what is available in the private sector. It is essential that this contribution should be accepted as fair by the public generally".

The following paragraph would then begin:

> "The Government therefore wishes ....".

3. Our other points are on the background brief and are purely factual. First, the word "many" should be deleted from the second paragraph. We do not know of any local authority or nationalised industry pensions which are not index-linked. Second, the fourth paragraph might better read:

> "A large collection of "official pensions", mainly but not exclusively central and local government employees, are covered by the 1971 Pensions (Increase) Act, read in conjunction with other pensions legislation, notably the Social Security Pensions Act 1975. Official pensions are increased in line with forecast movements of the retail price index, at the same time and by the same amount as the

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additional component of long term social security benefits (the State Scheme). Other public sector schemes provide similar inflation-proofing, but rest on different legislation or agreements".

4. The Minister of State has also seen the letter of 20 March from the Minister of Transport to the Chancellor. He believes that the Government could not defend an inquiry which excluded the nationalised industries, whose employees form a large proportion of prospective beneficiaries of index-linked pensions. As they stand, the terms of reference are not unduly restrictive and the inquiry would not be precluded from considering the effect of present practice on nationalised industry prices: indeed, they might be expected to take this point at an early stage of their work. Questions about how adequately contributions reflect the security provided by inflation-proofing would seem to apply with equal force to the nationalised industries and the public services, because they go beyond strict actuarial valuation. The Minister of State thinks however that a small ambiguity in sub-paragraph (a) of the terms of reference could usefully be removed by the substitution of "where he assesses" for "in his assessment of", to make it clear that the Government Actuary is not responsible for valuing all public sector schemes.

5. I am sending copies of this letter to Tim Lankester, Don Brereton, Ian Ellison and Richard Dykes.

Yours sincerely

Gary Rogers

G D ROGERS
Assistant Private Secretary

MR. LITTLER

cc: Chief Secretary
Financial Secretary
Minister of State (C)
Minister of State (L)
Sir Douglas Wass
Sir Anthony Rawlinson
Mr. Ryrie
Mr. Bailey
Mr. F. Jones
Mr. Dixon
Mr. Kemp
Mr. Unwin
Mr. Rayner
Mr. France
Mr. Cropper
Mr. Ridley
Mr. Cardona

PS/Prime Minister

25/3

INDEX-LINKED OCCUPATIONAL PENSIONS

As agreed when the Chancellor saw him on 19 March, I telephoned Sir Rowland Wright on Sunday evening to learn of his decision. Sir Rowland said that with the utmost reluctance he had to report that his present burden of work made it impossible for him to give to this task the serious attention it clearly deserved. Tempted though he was, therefore, he felt he must decline. He did however suggest that either Alex Jarratt or Lord Plowden would be excellent candidates. He did not think that the fact that they had both been public servants was an adverse factor. On the contrary, it made them familiar with both sides of the argument. Either could be relied upon to be totally objective. He had taken the liberty of sounding out Lord Plowden in very general terms. The latter had shown considerable keenness to take on the job, particularly as many of his present commitments were drawing to an end.

2. Since neither of these possibilities particularly attracted either the Chancellor or the Prime Minister, the Chancellor considered the list in your minute of 21 March. He thought Sir Bernard Scott would be a good candidate, but the Prime Minister's preferred list, in order, was Sir Alastair Pilkington, Sir Adrian Cadbury, and Campbell Fraser. On the Chancellor's instructions I put the idea to Sir Alastair Pilkington on the telephone. He was categorical in saying that he had at present too many commitments to be able to consider taking the job on.

/He was

He was Executive Chairman of Pilkingtons until September, and also a non-executive Director of Chloride, a post he intended to retain after September. It was, however, clear that his view might well be different if the post were to be offered to him in the autumn.

3. I am now consulting the Chancellor about how to proceed. It looks, however, as though we shall be unable to name the Chairman in the Budget Speech, particularly in view of late complications raised by other Ministers.

(M.A. HALL)
24th March 1980

Econ Pol

10 DOWNING STREET

TIM

Jeff Littler rang and suggested a revised amendmet:

"... to take into account in determing pay and other conditions of service"

MS

Pilkington has turned it down

MS

3pp's

PRIME MINISTER

NBPM

Pr. 2/7/3

INDEX LINKED OCCUPATIONAL PENSIONS

I have a few comments on the proposed independent inquiry into the value of index-linked pensions in the public sector.

So far as the members are concerned I agree that of the people from the insurance industry Mr Gordon Bailey would be a very good choice. If he was unable to serve I regard Mr R E Holland as the next best. The Secretary of State for Industry's suggestion of Mr Harold Rose also has attractions, but if we are to show that the inquiry is independent we should perhaps avoid both known opponents and likely supporters of the present arrangements.

My main concern springs from my responsibility for the NHS in which the staff, including the doctors and dentists receive index-linked pensions. The inquiry might well be expected in the Civil Service, which has been the main object of public criticism of index-linking, but it will come as a surprise to NHS staff and may cause some trouble. It might help if, in announcing the inquiry, assurances could be given that staff interests will be able to submit evidence to the committee and that there will be consultations with staff interests before the committee's recommendations are implemented.

Turning to the proposed terms of reference I am not sure that the special position of the Doctors and Dentists Review Body is sufficiently recognised in sub-paragraph (d). As you know, the Review Body makes recommendations to you, and there are no negotiations as there are, for example, in the Civil Service following the reports of the Pay Research Unit. Perhaps the point could be met by amending the sub-paragraph to read:

"(d) to report their conclusions and suggest what valuations or methods of valuation would be appropriate to take /account/ of them in considerations of public sector pay and other conditions of service."

This would also take account of the general point that the conclusions might point towards changes in superannuation contributions rather than in pay.

I also feel that the inclusion in the terms of reference of relative job security seems odd. I am not clear whether this inquiry is to consider the weight to be given to job security in considering pay or in the value of index-linked pensions. If the intention is to cover the former I wonder whether we would be wise to complicate the Committee's work of examining the value of index-linked pensions, in itself difficult enough, with another issue which, at first sight, is not crucial to the Committee's main task? In any event we would, I think, need to explain the purpose of this part of the terms of reference more fully than in the draft explanatory note (Annex C to the Chancellor's minute).

I am copying this minute to the recipients of the Chancellor's minute.

PJ

24 March 1980

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

CONFIDENTIAL

PL
25/3

The Rt Hon Sir Geoffrey Howe MP
Chancellor of the Exchequer
Treasury
Treasury Chambers
Parliament Street
LONDON SW1

20 March 1980

Dear Geoffrey

INDEX LINKED OCCUPATIONAL PENSIONS

Your minute to the Prime Minister of 6 March invited comments on the proposed membership and Terms of Reference of the inquiry into index linked occupational pensions in the public sector. My only comment on the proposed membership of the inquiry is that I too think it would be wise to have at most one member who is or may be a recipient of an index linked pension. The terms of reference and explanatory notes seem, however, to have been written with an inquiry confined to public service pensions in mind rather than one ranging also over the whole of the public sector including the nationalised industries. This is perhaps because our discussions in E on 20 February centred round the narrower rather than the wider field.

I do not think an inquiry with the terms of reference proposed would help us in dealing with nationalised industry pensions. The industries in general have funded pension schemes. The rules, which in many cases provide directly for indexation of one sort of another, are administered by trustees. The adequacy or otherwise of contributions is a matter for the trustees to assess on the advice of their actuaries. Only in a minority of cases is the Government Actuary retained for this work. The schemes, like private-sector occupational pension schemes, are subject to the general supervision of the Occupational Pensions Board. It is a nice question how far the pension funds and their trustees can be regarded as operating in the public sector. Our

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denationalisation measures will leave beneficiaries under the schemes in the industries affected with the same rights as now. On this account also the boundary between public and private sector in this area is blurred.

A clear public sector interest arises only if contributions are judged inadequate or funds are mismanaged so that a nationalised industry has to make up deficiencies out of its revenues. In that case there may be a downward pressure on pension benefits or pay. Alternatively, there may be an effect on the industry's prices or its borrowing requirement. In an extreme case the industry may turn to the Government for specific help. None of the sub-paragraphs in the terms of reference proposed seem to bear on a situation of this kind.

The choice seems to me to lie between extending the terms of reference in some suitable way - for example by asking the inquiry to look at the effect of current practices on nationalised industry prices - or excluding the industries, initially at least, from the ambit of the inquiry. Because of the extra complexities involved there seems to me to be a good deal to be said for the latter course.

One sentence in the Explanatory Note as it stands gives me particular cause for concern. As you know, the Transport Bill, which has just completed its Committee Stage in the Commons, proposes, inter-alia, new arrangements for Government support for the BRB and NFC pension funds. As I said in my letter of 31 January some concern has been expressed that if the Government decided to stop indexation of public service pensions the new support system would make it easier to stop supporting the indexation of railway and NFC pensions. The reference in paragraph 3 of the draft Explanatory Note that the Government "reserves for future consideration whether it is right to continue present arrangements ...." could therefore cause problems during the remaining stages of the Bill and I would much prefer to see it either dropped or amended to make it clear that interference with the rights of beneficiaries under existing trusts are not contemplated.

I am sending a copy of this letter to the recipients of yours.

Yours ever

Norman

NORMAN FOWLER

21 MAR 1989

Mr ~~Lankester~~
Spoke Wiggins.
Request for draft PQ by close of play taken aboard.
NG 21-3

CONFIDENTIAL

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

T Lankester Esq
Private Secretary to the
Prime Minister
No 10 Downing Street

20 March 1980

Dear Tim

TL 25/3

INDEX-LINKED OCCUPATIONAL PENSIONS

Further to your letter of 18 March, the Chancellor met Sir Rowland Wright yesterday, offering him the job of Chairman. Sir Rowland was obviously attracted by the possibility, but said that there were heavy and exceptional demands on his time at the moment because his firm - Blue Circle Cement - had just been referred to the Monopolies and Mergers Commission. He would however think the matter over and let us know by the end of the week-end. I will report further.

... Meanwhile, the Treasury have drafted the enclosed Press Notice, with which the Chancellor is content, including the passage in the notes to editors in square brackets. The intention would be that this would be released by No 10, and would be referred to in the Budget Speech. We should welcome your early reactions.

I am copying this letter to Don Brereton, Ian Ellison, Richard Dykes and Geoffrey Green.

Yours ever,

M A HALL
Private Secretary

/

DRAFT PRESS NOTICE

ENQUIRY INTO VALUE OF PENSIONS

The Prime Minister has appointed as Chairman of an independent enquiry to consider the value of index-linked occupational pensions which are widely provided in the public sector. The names of other members of the enquiry team will be announced later. It is hoped that the enquiry can be completed within 3 or 4 months. The terms of reference are attached.

NOTES TO EDITORS

This is the enquiry referred to in the Chancellor's Budget Speech today.

2. The Government is concerned about the arrangements for index-linked occupational pensions almost throughout the public sector, which are not matched by occupational pensions in the private sector. The difference of pension treatment and its cost have become important as a result of several years of high rates of inflation, and has attracted strong criticism. The Government is dedicated to the objective of reducing inflation, and success in that will diminish the problems arising from different kinds of pension treatment. Nevertheless, those problems do at present exist, and need urgent consideration.

3. Pension schemes and the benefits attached to them involve long-run expectations and commitments which should not lightly be interfered with. The Government is conscious of the obligations it has inherited towards its own direct employees and other employees in the public sector. The Government nevertheless reserves for future consideration whether it is right to continue present arrangements for full inflation-proofing of most public sector occupational pensions against the background of national economic and social considerations.

/4.

4. First, however, the Government wishes to explore more thoroughly the question whether the additional advantages of index-linked pensions can be adequately valued, and their additional value translated into an appropriate level of employee contributions. This is the purpose of the proposed enquiry.

5. [The terms of reference specify two particular elements in valuation which seem to be worth attention: first, one which arises only where (as in the case of the non-industrial Civil Service and some other public sector groups) a deliberate attempt is made to cost the effect of inflation-proofing for future years; the other an attempt to get at the elusive problem of valuing security in an uncertain world. The opportunity is taken to invite those conducting the enquiry to consider also the problem which is in some ways parallel, that of relative job security.]

TERMS OF REFERENCE

Having regard to the need to ensure that full account is taken in all areas of the public sector, whether by contributions or salary abatement, of the value of inflation-proofing of occupational pensions, and of relative job security, taking due account of arrangements in the private sector:

(a) to consider the assumptions and methods used by the Government Actuary in his assessment of the value of differences in inflation-proofing;

(b) to consider the relative degree of security in the full inflation-proofing enjoyed by public sector employees compared with those in the private sector, and the additional value to be placed upon it;

(c) to consider how to assess the relative job security enjoyed by employees in the private and public sectors;

(d) to report their conclusions and suggest what valuations or methods of valuation would be appropriate to take account of them in pay negotiations.

BACKGROUND BRIEF

Representations

A further announcement will be made when the team for the proposed enquiry has been completed. That announcement will indicate arrangements to receive representations.

What Public Sector Pension Schemes are Index-Linked?

Nearly all, which makes a very long list, including Civil Service, Ministers, Members of Parliament, Judiciary, Armed Forces, Police, Nurses, Doctors, Teachers, and many local authority and nationalised industry employees. In total, some 5½ million present employees in the public sector are covered by index-linked pension schemes.

Details of Schemes

Details vary, and enquiries should be referred to the managements of the particular public sector groups concerned.

Basis of Present Index-Linking

A large collection of "official pensions", mainly but not exclusively central government employees, are covered by the 1975 Pensions Increase Act, read in conjunction with other pensions legislation. These provide a link to the Retail Price Index, calculated annually. Other public sector schemes operate similar linkages, but rest on different legislation or agreements.

Cost

No figures can be given. (Global figures are not available because there is no central knowledge of the costs of a large number of schemes under different managements within the public sector. Even for any particular scheme, the definition of cost can only be given in relation to some alternative system; there are also problems in interpreting the cost in any particular year.)

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Prime Minister

The enquiry will be trailed in the Budget Speech. The Chancellor is going to suggest that you – as Minister for the Civil Service – formally announce the enquiry in a Written Answer.

T.
25/3

CONFIDENTIAL

CHANCELLOR OF THE EXCHEQUER

INDEX-LINKED OCCUPATIONAL PENSIONS

I have seen a copy of your minute of 17 March to the Prime Minister, and a copy of her Private Secretary's reply of 18 March to yours.

I believe Rowland Wright would be an excellent choice as Chairman if he can be persuaded to take the job on.

As between Andrew Bain and Harold Rose, my preference would be Bain. The Committee's enquiry must clearly be searching if it is to carry conviction with the private sector. On the other hand, we must ensure too that it commands confidence among millions of people in the public sector who are beneficiaries of the present arrangements. I do not think we should have people who are known to be strongly opposed to the existing system, any more than we should have people who are biased in its favour. It must be seen to be clearly impartial.

I would marginally prefer Alex Jarratt to Alan Lord - mainly because his Civil Service experience is more remote. It is only a short time since Alan Lord left the Treasury and he would still be very closely identified with the Civil Service. But I would be happy with either.

I am copying this to the others who received your minute of 6 March.

P.C.

PAUL CHANNON
20 March 1980

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CONFIDENTIAL

20 MAR 1980

CONFIDENTIAL

CONFIDENTIAL

Econ Pol

ds

10 DOWNING STREET

From the Private Secretary

cc HO, FCO, D/IND, LPO, D/M, MAFF, DOT, D/N, CSO, LCO, MOD, SO, DHSS, DES, PGO, CSD, D/TRANS, CO

18 March 1980

Index-Linked Occupational Pensions

The Prime Minister has read the Chancellor's further minute of 17 March on the above subject, and agrees that he should approach Sir Roland Wright to see if he would be willing to be Chairman. As regards the choice of someone with mixed public and private sector experience, the Prime Minister is neutral as between Sir Alex Jarratt and Mr. Alan Lord.

I am sending copies of this letter to the Private Secretaries to the members of E, Ian Maxwell (Lord Chancellor's Office), Brian Norbury (Ministry of Defence), Godfrey Robson (Scottish Office), Don Brereton (Department of Health and Social Security), Peter Shaw (Department of Education and Science), Richard Prescott (Paymaster General's Office), Geoffrey Green (Civil Service Department), Genie Flanagan (Department of Transport) and David Wright (Cabinet Office).

I. P. LANKESTER

Martin Hall, Esq.,
HM Treasury.

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Z PB

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Prime Minister

Agree the Chancellor should approach Rowland Wright?

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

PRIME MINISTER

Yes

INDEX-LINKED OCCUPATIONAL PENSIONS

Your own and other comments on my minute to you of 6th March on this subject have raised one difficult question on the list of candidates: the question of including or not people who might have a personal interest through their own past public service and pension entitlements from it.

2. Like Paul Channon, I do not think this need debar us from including somebody with such experience as a member, but I agree on reflection that it might be wise to avoid this in the Chairman. The name of Rowland Wright has been suggested to me as a possible Chairman without any public sector background, and I think he would indeed be a good choice.

3. If we were able to get Rowland Wright as Chairman, your preferences for Andrew Bain (or indeed Keith Joseph's suggestion of Harold Rose), Leif Mills and Gordon Bailey would make excellent first choices under those headings. None of these four would be directly connected with the public sector, which would leave us free to bring in some mixed public and private sector experience for the last member. I would be well content with your preference of Alan Lord. It would not, I think, be appropriate to ask Lord Plowden to serve as a member, but I wonder whether you would see Alex Jarratt as preferable to Alan Lord, if available, on the ground of a rather more equal balance between his public and private sector experience. I had given some thought to the possibility of someone from either local government or a nationalised

/industry

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CHANCELLOR OF THE EXCHEQUER

industry, who would be an alternative to Lord or Jarratt. Good candidates from these fields are certainly not obvious, and I could not think of any who would contribute more or make for a better balance.

4. It would obviously be an advantage to have settled at least the Chairmanship before we announced the enquiry. If you are attracted by the idea of Rowland Wright, would you like me to sound him?

5. I am copying this to others who received my original minute to you.

G.H.

(G.H.)

17 March, 1980

CONFIDENTIAL

Econ Pol.

SECRETARY OF STATE FOR THE ENVIRONMENT

2 MARSHAM STREET
LONDON SW1P 3EB

My ref:

Your ref:

File with Tim

13 March 1980

Dear Geoffrey

INDEX-LINKED OCCUPATIONAL PENSIONS

Thank you for sending me a copy of your minute of 6 March to the Prime Minister.

I have no comments on the suggested names for the inquiry.

Insofar as the terms of reference are concerned, I assume that these would pick up the differing retirement ages in the public and private sector, where this applies.

I am copying this letter as before.

yours ever

Michael

MICHAEL HESELTINE

The Rt Hon Sir Geoffrey Howe MP

CONFIDENTIAL

JU

Pm has seen

PRIME MINISTER

INDEX-LINKED OCCUPATIONAL PENSIONS

I should like to comment briefly on the Chancellor of the Exchequer's letter and enclosure of 6 March about the proposed inquiry.

On the immediate question of names, I suggest that one really needs to include an iconoclast if the public are to be reassured of our determination to take a hard look at this subject. Harold Rose would be an obvious choice as he could combine authority with a known antipathy towards the existing pensions system. Ralph Harris would be a suitable alternative. Similarly I fear that the inquiry team would risk losing some credibility if it included members with a significant Whitehall background. In this respect I share the Chancellor's doubts about Alan Lord but even Alex Jarratt, with a Civil Service career spanning 24 years, might not escape criticism nor indeed would Edwin Plowden.

On presentation, you will recall E Committee's agreement that the inquiry should cover the whole of the public sector and we shall need to brief the inquiry team, and get across publicly, that we see this as extending to MPs pensions. Given the sensitivity of the House, the issue will need to be handled with some care and the Chancellor will be able to advise how best this can be achieved. One possibility would be for the Statement to say that the Report of the inquiry team will be submitted to the House

/by the ...

by the Government so that it can be taken into account in future reviews of MPs pay and pensions.

I am sending copies of this minute to those colleagues listed in paragraph 7 of the Chancellor's letter.

KJ

K J

12 March 1980

Department of Industry
Ashdown House
123 Victoria Street

cc Mr Duguid

Prime Minister

The point about not having too many people with current or prospective index linked pensions is a good one. The Chancellor will no doubt take this, and other (including yours), comments into account.

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PRIME MINISTER

INDEX-LINKED OCCUPATIONAL PENSIONS

I have seen the Chancellor of the Exchequer's minute of 6 March to you on this subject, the comments in Jim Prior's minute of 10 March, and your own, as recorded in Mr Lankester's minute of 10 March.

I agree with the Chancellor's proposed terms of reference. I also agree with him that we should not approach the Select Committee formally, but rather leave the initiative with them once the inquiry has been announced.

On the proposed membership of the inquiry, I think it would be best to limit cross-membership with the Pay Research Unit Board to one. Of the two candidates who are members of PRUB, my preference would be for Holland rather than Mills, unless, as I would myself consider, the latter is regarded as the most promising trade union candidate.

We must ensure that this Committee is not seen by the public to be a whitewash. Therefore I am worried about having too many people on the Committee who are prospective recipients of index-linked pensions. In particular, would it be wise to have a Chairman in this situation? Sir Alex Jarratt is a prospective recipient, and Lord Plowden is actually receiving an index-linked pension at the moment for his services as Chairman of the Atomic Energy Authority.

Mr Alan Lord, who left the Civil Service only three years ago after 27 years service, is also a prospective recipient of such a pension.

We must also bear in mind that academic economists have index-linked pensions, as do present and former MPs, including

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Lord Diamond. I do not suggest that all these should necessarily be excluded, but I would have thought that we ought to have on the Committee no more than one person who is personally affected in this way - and, in my opinion, he should not be the Chairman. Otherwise, I am afraid that we will run the risk of the inquiry getting off on the wrong foot.

I am copying this to the recipients of the Chancellor of the Exchequer's minute.

P.C.

PAUL CHANNON
12 March 1980

2

Prime Minister

To note. (I have passed on your comments - including your preference for Leif Mills over David Lea).

T 10/3

CHANCELLOR OF THE EXCHEQUER

MG

INDEX-LINKED OCCUPATIONAL PENSIONS

I am content with all the names for the inquiry suggested in the annex to your minute to the Prime Minister of ~~6~~ 7th March and with the balanced composition you propose.

I think it essential to have a trade union member and would prefer David Lea to Leif Mills. The former is more able and could be expected to provide a more representative view of employee interests. I suspect that Leif Mills might have the interests of his members in banking too much in mind.

If Alan Lord were thought to be disqualified, I would give preference to Lord Diamond over Peter Gibson.

I am also content with the terms of reference proposed.

As for the time the inquiry might take, it seems to me essential that we give unions and other interests the opportunity of making representations. This could be critical to the reactions to its findings and their implementation. I nevertheless share the hope that the inquiry could be completed within a few months.

I am copying this minute to the Prime Minister and to the other recipients of yours.

J P
10 March 1980

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Jfh

CC HO C.SEC.
FCO LCO
IND MOD
LPO SO
EMP DHSS Econ Pol.
MAFF PGO
TRADE CSD
ENG TRANS
CO

10 DOWNING STREET

From the Private Secretary

10 March 1980

Index-linked Occupational Pensions

The Prime Minister has read the Chancellor's minute of 6 March on the above subject. She has the following comments on the names for the inquiry suggested in annex A of the minute.

She doubts whether it would be right to appoint Sir Alex Jarratt as Chairman, even though he would make an excellent one, given that he is a former civil servant and therefore might not be thought to be wholly impartial. She thinks Lord Plowden would be a good choice.

Of the other suggested members, she thinks Mr. Gordon Bailey would be excellent; under the other three headings, her preference would be for Mr. Leif Mills, Mr. Andrew Bain and Mr. Alan Lord.

The Prime Minister has also commented that perhaps the Chancellor ought to consider including someone from either local government or a nationalised industry since both have pensions which are inflation-proofed.

I am sending copies of this letter to the Private Secretaries to members of E Committee, to Ian Maxwell (Lord Chancellor's Office), Brian Norbury (Ministry of Defence), Godfrey Robson (Scottish Office), Don Brereton (Department of Health and Social Security), Richard Prescott (Paymaster General's Office), Geoffrey Green (Civil Service Department), Genie Flanagan (Department of Transport) and David Wright (Cabinet Office).

T. P. LANKESTER

A.J. Wiggins, Esq.,
HM Treasury.

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DJ

2pps

Prime Minister
Content with the suggested names in Annex A subject to the points below?
JL 7/3

Ref. A01638

PRIME MINISTER

Index-linked Occupational Pensions

I have seen the Chancellor of the Exchequer's minute of 6th March about the proposed inquiry.

2. I have no doubt that Sir Alex Jarratt would be an admirable Chairman; but I doubt whether we should appoint a former civil servant who might be thought to be not wholly impartial on the subject. Although Lord Plowden is over 70, he is in very good shape, and I should have thought that his public sector experience is so far in the past as not to disqualify him.

3. There ought to be one former public servant on the body, I suggest; and there could be nobody better than Mr. Alan Lord, who is one of those proposed as the possible fifth member.

RTA

ROBERT ARMSTRONG

7th March, 1980

I have indicated my own preferences under each heading. But ought not we to have someone from either Local Govt. or a Nationalised industry. Both have inflation-proofing.

MT.

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

PRIME MINISTER

INDEX-LINKED OCCUPATIONAL PENSIONS

We agreed at the expanded meeting of E Committee on 20th February to go ahead with my proposal for an independent inquiry into the value of the right to inflation-proofed pensions in the public sector.

2. I suggest that we aim to announce the inquiry either on Budget Day or the day after (when Patrick Jenkin will be announcing the detailed social security payment changes). I think it would be right for the inquiry to be set up and the members appointed formally by you, and that the announcement should therefore come from your Office. I will arrange for a draft to be prepared a little nearer the time.

3. Meanwhile, the most urgent step is to decide upon, and recruit, a team of people for the inquiry. I attach at Annex A a note on the shape of a 5-man team and suggestions of names. I would welcome any additions or comments. Subject to that, you may like to leave it to me to approach possible candidates.

/4. I also

... 4. I also attach, at Annexes B and C, a slightly revised draft of the formal terms of reference which I would suggest for the inquiry, and an explanatory note indicating the line which should be adopted in explaining the purpose of the inquiry to candidates, and I envisage that we would draw on some of this material for explanations in our public announcement.

5. You will remember that, as regards publicity, we also talked at E Committee about the possibility of bringing in a Parliamentary Committee, not confined to the question of valuation for contributions, but on the subject of inflation-proofed pensions more widely. The appropriate Committee must, I think, be the Treasury and Civil Service Committee (we would of course need to make it particularly clear to them that we were not just concerned with the Civil Service). On reflection, however, I doubt the wisdom of our putting the question formally to the Committee: to do so might make it difficult for us to avoid taking a position on the merits of "inflation-proofing". We cannot avoid some awkward questions in any case, but I conclude that our best course would be to ensure that our decision to set up an inquiry is brought to the attention of the Committee, and to encourage the Committee discreetly to take the initiative itself in pursuing the subject. If you agree, this could readily be arranged through our normal contacts with the Committee, at the time.

/6. To conclude, I

6. To conclude, I would be grateful for early comments on the suggested names for the inquiry, and to know whether you would like me to approach them. Any comments on the proposed terms of reference and public presentation can be taken at more leisure.

7. I am copying this letter and the enclosures to other Members of E Committee, other colleagues who were present at the discussion on 20 February, (the Lord Chancellor, the Secretaries of State for Defence, Scotland, Social Services and Education, the Paymaster General, Minister of State, Civil Service Department, and the Minister of Transport), and to Sir Robert Armstrong.

(G.H.)

6 March 1980

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ANNEX A

MEMBERSHIP

It is thought desirable to have a chairman plus four members, with distinction and collective breadth of experience. The chairman might best be an industrialist with varied past experience; a reasonable balance might be achieved if he were supported by another man with wide management experience, a leading figure in the insurance industry, an economist and a trade unionist. The idea of one member being a public service employer is attractive, but such a man is likely to be a beneficiary himself of a substantial inflation-proofed pension of the kind under discussion. It is also desirable to have some cross-membership with the Pay Research Unit Board, and/or the Clegg Commission and/or Review Bodies.

2. Some spare names will be needed for the list of candidates to be approached. The following is a suggested list.

Chairman

Alex Jarratt (Chairman of Reed International, formerly National Board for Prices and Incomes and a civil servant, a respected leading member of the CBI).

✓ Lord Plowden (a good mixture of public and private sector experience, an experienced chairman and currently a member of the Top Salaries Review Body).

Members

3. From the insurance industry, we do not want a professional actuary but a leading figure in the industry (most of whom, as it happens, have been actuaries). The following four names are suggested:

R.E. Holland (Chief General Manager of Pearl and a prospective member of the PRUB).

✓ Gordon Bailey (National Provident, past President of Institute of Actuaries, member of Wilson Committee and well-known and highly respected in the City).

Excellent

Bob Macdonald (Scottish Provident, former President of Faculty of Actuaries).

Ron Peat (General Manager of Legal and General).

Trade Union Member

4. The two names suggested are:

✓ Leif Mills (NUBE and a Member who has worked reasonably effectively on the PRUB).

David Lea (Deputy Secretary General of the TUC).

Economist

5. Two academic economists who have shown particular interest in pensions from various points of view are:

✓ Andrew Bain (Edinburgh, Member of Wilson Committee).

Michael P Fogarty (Centre for Studies in Social Policy, London).

An alternative would be to seek an older general economist of high reputation, such as Sir Alec Cairncross.

Other Member

6. Possibilities might include:

Peter Gibson (formerly BP, a Member of the Clegg Commission suggested for that by the CBI).

Lord Diamond

✓ Alan Lord (Dunlop, formerly Treasury, who might be disqualified by his own pension position, but could be expected to make a vigorous contribution to discussion).

DRAFT TERMS OF REFERENCE

Having regard to the need to ensure that full account is taken in all areas of the public sector, whether by contributions or salary abatement, of the value of inflation-proofing of occupational pensions, and of relative job security, taking due account of arrangements in the private sector:

(a) to consider the assumptions and methods used by the Government Actuary in his assessment of the value of differences in inflation-proofing;

(b) to consider the relative degree of security in the full inflation-proofing enjoyed by public sector employees compared with those in the private sector, and the additional value to be placed upon it;

(c) to consider how to assess the relative job security enjoyed by employees in the private and public sectors;

(d) to report their conclusions and suggest what valuations or methods of valuation would be appropriate to take account of them in pay negotiations.

/10

EXPLANATORY NOTE

The Government is concerned about the arrangements for inflation-proofed occupational pensions almost throughout the public sector, which are not matched by occupational pensions in the private sector. The difference of pension treatment which might have attracted little attention or criticism in other circumstances has become large and important as a result of several years of very high rates of inflation. The Government is dedicated to the objective of reducing inflation, and success in that will diminish the problems arising from different kinds of pension treatment. Nevertheless, those problems do at present exist, and need urgent consideration.

2. There are two sides to the arrangements for occupational pensions: the scale of benefits provided and the scale of contributions, particularly those made by employees, towards the value of their future pensions. Equity could be sought by bringing benefits more closely into line with each other, but could also be obtained, although in different form, with differing expectations of benefit matched by different employee contributions. There is indeed already an element of differential contribution in some public service schemes, explicitly but perhaps not adequately taking account of benefits to be expected, especially the benefits of full inflation-proofing.

3. Pension schemes and the benefits attached to them involve long-run expectations and commitments which should not be lightly interfered with. The Government is conscious of the obligations it has inherited towards its own direct employees and other employees in the public sector. The Government nevertheless reserves for future consideration whether it is right to continue present arrangements against the background of national economic and social considerations. First, however, the Government wishes to explore more thoroughly the question whether the additional advantages of the kind of inflation-proofed pension enjoyed in the public sector can be adequately valued and that value translated into an appropriate level of employee contributions. This is the purpose of the proposed enquiry.

4. The terms of reference specify two particular elements in valuation which seem to be worth attention: first, one which arises only where (as in the case of the non-industrial Civil Service and some other public sector groups) a deliberate attempt is made to cost the effect of inflation-proofing for future years; the other an attempt to get at the elusive problem of valuing security in an uncertain world. The opportunity is taken to invite those conducting the enquiry to consider also the problem which is in some ways parallel, that of relative job security.

5. It is hoped that the enquiry can be completed within a few months.

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Submitted in E folder.
Elan Bol

PAYMASTER GENERAL

PRIVY COUNCIL OFFICE
WHITEHALL, LONDON SW1A 2AT

19 February 1980

The Rt Hon Sir Geoffrey Howe QC MP
The Treasury
Whitehall
SW1

Dear Chancellor,

1 I have studied your paper E(80)16, containing proposals for a possible modification of pensions increase to give full increase on the first £1000 of pension and a lower percentage on the balance.

As my Office (PGO) are the biggest payers of occupational pensions (about a million by the time the next pensions increase is due) I feel I should draw colleagues' attention to the administrative difficulties which this suggestion would create.

2 The problem arises where two or more pensions are payable to the same person. In such circumstances there are two possible courses open:-

(a) full increase could be permitted on the first £1000 of each pension

(b) full increase could be permitted on the first £1000 of the combined pensions.

3 There are numerous instances of pensioners having multiple pensions, eg:

Scottish and English teachers' pensions;

Forces pensioners with subsequent employment, eg as Civil Servant, Teacher or National Health Service;

Forces and police or fire brigade;

Civil Servants who after retiring with a frozen pension return to the Civil Service and elect to have a second pension;

and several others.

In the National Health Service, former Consultants to several hospitals often draw a separate pension for each Consultancy.

4 IF COURSE (a) IS ADOPTED

(i) In all these groups the pensioner will receive full increase on £1000 for each pension thus benefitting compared with the person with the single pension.

(ii) The final example of the NHS would be the most difficult to defend and to deal with. The Consultant may have 5 or 6 separate pensions each

/of

of which will qualify for full increase on the first £1000. Under the present Pensions Increase Scheme, where a standard percentage applies throughout, the PGO computers hold only the total figure payable without details of its make up. A pension of £6000 might be a single pension qualifying for full increase on £1000 or a 3 part pension qualifying for increase on £3000 or a 3 part pension qualifying for increase on £2970 because 1 part is only £790 a year. Considerable research into old records would be necessary to determine the make up of every pension in payment and to ensure that proper entitlement is paid. In view of the case of Colonel Ottway this research could not be skimped.

5 IF ALTERNATIVE (b) IS ADOPTED

(i) The main difficulty of this course is the problem of finding out if pensioners have more than one increasable pension. In some double pension cases both parts would be paid by the PGO perhaps from different Votes (eg Forces and Civil Service), but the computer records are not cross-referenced. In many cases different authorities may pay the two parts (eg Teachers and Local Authorities, Forces and Firemen).

(ii) The only possible method of determining what pensions each pensioner is receiving is to send out an enquiry to all the 1,000,000 people on PGO's books.

For every reply showing multiple pensions it will be necessary to write to the other Paying Authority to agree what increase is due and how it is to be apportioned. Only then can the increase be calculated.

The existing computer programs which, on a single run, award increase automatically to all cases with entitlement could not be used. Extensive reprogramming would be needed which with the limited resources available could not be completed in time for the 1980 increase.

(iii) A similar problem arose when the Pensions (Increase) Act 1952 awarded a flat rate increase which had to be apportioned over all the pensions payable. It took nearly a year to pay the increases to all pensioners and that would not now be acceptable.

6 CONCLUSION

Course (a) would mean recruiting a substantial number of clerks and training them to undertake the research into the make up of each pension so that the further increase on multiple pensions

/could

The Rt Hon Sir Geoffrey Howe QC MP (contd.) 19.2.80

could be paid manually.

Course (b) would involve computer programs which could not be prepared in time, or an increase in clerical staff which could neither be recruited nor trained in time. The problem would, of course, not be confined to the PGO; all pension paying bodies within the public sector would be similarly affected.

It is clear that either course would involve injustice to some pensioners and considerable administrative difficulty and expense.

I conclude that your first proposal is, from my Department's point of view, impractical.

I am copying this to members of E Committee, and Patrick Jenkin, Francis Pym, George Younger, Mark Carlisle, Norman Fowler, Paul Channon and Sir Robert Armstrong.

Yours sincerely

Richard Prescott

ANGUS MAUDE

(Approved by the Paymaster General and signed in his absence)

19 FEB 1980

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Ref. A01475

PRIME MINISTER

Inflation-proofed Pensions

(E(80) 16 and 18)

BACKGROUND

E(80) 2nd Mtg Item 2,

At the last discussion on 23rd January (E(80) 1st Meeting, Item 5) the Committee considered a proposal by the Chancellor of the Exchequer that a group of "wise men" should be asked:-

— January 15

(a) To comment on the economic assumptions used by the Government Actuary in valuing public service pensions.

(b) To set a subjective price on the "guarantee" of index-linking enjoyed by public service pensioners.

(c) To advise how "job security" might be valued.

2. The Committee deferred a decision because of the doubts expressed by Sir Kenneth Berrill about the wider effects of a change in the Government Actuary's assumptions on the real return on investment for the occupational pensions industry.

3. The point raised by Sir Kenneth Berrill is discussed in Annex 2 to the Chancellor's paper E(80)16. This suggests that a change in the economic assumptions - especially the assumed real rate of return on investments - could have a significant effect on the liabilities of existing pensions funds (paragraph 6 of Annex 2 equates a 1 percentage point reduction in the assumed rate of return with £1 billion extra annual contributions in the private sector and £½ billion in the public sector) but doubts whether relatively small changes in the assumptions would have much effect in practice. It is a question of degree: small changes would not cause problems but would not save much money; big changes could be very damaging but are unlikely because the Government Actuary's assumptions are in the middle of the range adopted by his professional colleagues elsewhere.

4. The main thrust of the Chancellor's paper is to argue for a limited degree of deindexing of public service pensions for two years "during which we could try to work out a more satisfactory long-term arrangement" (paragraph 3 of E(80) 16).

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Unfortunately the Chancellor nowhere explains what sort of review he has in mind - though given the wide range and complexity of public sector pension schemes, it is to be doubted whether anything less than a Royal Commission would be able to do the job satisfactorily or carry conviction.

5. In addition to limiting his proposals to a two-year period, the Chancellor also advocates:-

(a) Limiting deindexing to those in receipt of public service pensions to the amount by which the pension exceeds £1,000 per annum.

(b) Excluding the nationalised industries even where, as in the case of the Post Office and British Rail, the pensions paid are subject to the provisions of the 1971 Pensions Increase Act.

6. The Minister of State, Civil Service Department's paper argues strongly against the Chancellor's proposals. His arguments are mainly political - the numbers of people involved, past commitments and the anomalies the Chancellor's proposals would create - for instance, that they would penalise soldiers, policemen and nurses but not gas workers, postmen, bus drivers or coalminers - or their senior staffs. He also points out that action on "contributions" would bring a much greater return to the Exchequer (£200 million a year for each 1 per cent additional contribution) than would the Chancellor's proposals (£50 million a year if the £1,000 cut-off is used, or £100 million a year if all public service pensions were cut).

7. In addition the Paymaster General has sent you a note on some of the mechanical problems to which the Chancellor's scheme would give rise. It suggests that the idea of a cut-off at £1,000 a year is administratively impracticable.

8. You will want to try and bring this particular subject to a conclusion at this meeting. To this end you might want to take your colleagues through the following questions:-

(a) Are "deindexing" and "increased contributions" mutually exclusive? Mr. Channon argues that they are (on the grounds that you cannot ask people to pay more for a "guarantee" which manifestly they would not have). The Chancellor is equivocal but appears to think it may be possible to deindex first and seek to raise contributions afterwards. Mr. Channon appears to have a certain logic on his side: it is not easy to see how one could ask people to contribute more for the certainty of the index link at the moment when legislation was being passed to remove that certainty. A prior decision here would simplify the rest of the discussion.

(b) Is deindexing politically achievable? It requires legislation: would the legislation carry enough support?

(c) Assuming that deindexing remains an option, do the Committee:

(i) Agree that it should be limited in amount and time as suggested by the Chancellor (up to 5 percentage points a year for two years)?

(ii) Agree that it should be applied only to the better off pensioners? The key questions here are perhaps justification - the better off have contributed in proportion to that pay, no less than those not so well off - and saleability to Parliament. The alternative is to deindex all public service pensions though this would enhance the anomalies referred to below.

(iii) Agree that the nationalised industries should be excluded despite the anomalies this would create? The problem is that many nationalised industry schemes are funded and not amenable to Government control.

(iv) Agree that the time bought should be used to examine public sector pensions in depth? If so, how should this be done? A Royal Commission?

(d) If attention concentrates on the "contributions" route do the Committee:-

(i) Think that "wise men" should be set to work at once? It is out of the question now that the "wise men" could report in time for their views to be taken into account in the negotiating timetable for this year's Civil Service pay round. But they could report for next year; or the CSD might seek to negotiate a temporary abatement in this April's pay settlement, so that any adjustment following the "wise men" could be implemented later in the year. The latter course would be akin to staging.

(ii) Think there is any other route? For example, could the idea of the "wise men" be dropped and a negotiation be entered into with the staff under which they would trade an abatement in pay this year (and in subsequent years) for a real guarantee of the preservation of index-linking? It could well be that, if asked, many civil servants would prefer to pay more for their pensions if by doing so they safeguarded index-linking. But is any Government able to give such a guarantee, given that what one Government does can be undone by its successor?

(e) How would any increased contribution by civil servants be reflected in other public sector schemes? These schemes vary enormously and while some may move by example, others will require a negotiated change with the unions concerned and/or legislation. A good deal of the basic factual information exists in Whitehall, and Ministers might find it helpful to commission a factual analysis as a basis for second-stage decisions.

9. Although you will no doubt wish to keep Ministers to the basic questions, a number of hares may well run. Points on these are:-

(a) Index-linked pensions cost civil servants only 2.6 per cent of salary. Not so. The 2.6 per cent represents the valuation of the difference between full index-linking and the 60 per cent index compensation achieved in the analogue schemes. Actual Civil Service contributions - partly through abatement of basic pay - are about 7 per cent. And we understand that the Government Actuary will be increasing his valuation of the extra index-linking this year to 3.8 per cent - making a total contribution in excess of 8 per cent. This compares with the 6 per cent contributed by Members of Parliament, the 5-6 per cent contributed by local government employees and the 5 per cent contributed by mineworkers. It will put Civil Service contributions at the upper end of the range of public sector practice.

(b) An index-linked pension is "priceless". True in the case of an individual trying to buy a pension from an insurance company. But misleading when large numbers are involved on a "pay as you go" basis. After six years of severe inflation the Government's contribution to this year's Civil Service pensions will be about 10 per cent of the wage bill. Comprehensive information is hard to come by, but a survey conducted for the TSRB and reported in their Tenth Report in 1978 (Table 9), showed that the average contribution by employers for the pensions benefits of senior executives in private industry exceeded 20 per cent of the salaries of those concerned, while the employee's contribution averaged 3 per cent. (The comparable averages in nationalised industries were 12.8 and 6.5.) Of course these figures relate to the better paid but we believe the 10 per cent Government contribution for all its staff to be no higher than the generality of private industry's contributions to its pension schemes.

(c) Index-linking gives disproportionate benefits to higher-paid public servants. Again hard information is difficult to come by but interesting tables are to be found on page 51 of TSRB 10. These show that, if superannuation benefits are measured in terms of lifetime salary, senior civil servants do rather better than their private sector counterparts - perhaps 20 or 25 per cent better - though the differences may be accounted for by higher contributions and lower retirement age. But the startling discrepancy is with senior officers of the Armed Forces and members of the judiciary whose pension "take" is almost double that of both their private and public sector counterparts. In the case of the Armed Forces the discrepancy almost certainly derives from the lower retiring age applicable to Service appointments.

HANDLING

10. You will want to ask the Chancellor of the Exchequer to introduce his paper and the Minister of State, Civil Service Department, to introduce his. Thereafter I suggest you might find it convenient to take your colleagues through the questions outlined in paragraph 8 above.

CONCLUSIONS

11. Very much subject to discussion, but probably emerging from the answers that your colleagues give to the questions you will pose. If the politics of deindexing are thought to be too difficult, a review by "wise men" of the value to be attached to the unquantifiable "guarantee" of index-linking for the purpose of calculating contributions would at least show that the Government was determined to look seriously at the problem, even if it could produce no results for this year's Civil Service pay round.

P.P. ROBERT ARMSTRONG

19th February, 1980

Percentage superannuation contributions for each type of post by type of organisation, by ranges of 1977 salary plus bonus, commission and profit sharing

All respondents (providing superannuation data)

Range of 1977 salary plus bonus etc	Chairmen				Deputy Chairmen				Main Board members				Senior executives			
	Private		Nationalised		Private		Nationalised		Private		Nationalised		Private		Nationalised	
	Employ-er's contri-bution	Employ-ee's contri-bution	Employ-er's contri-bution	Employ-ee's contri-bution	Employ-er's contri-bution	Employ-ee's contri-bution	Employ-er's contri-bution	Employ-ee's contri-bution	Employ-er's contri-bution	Employ-ee's contri-bution	Employ-er's contri-bution	Employ-ee's contri-bution	Employ-er's contri-bution	Employ-ee's contri-bution	Employ-er's contri-bution	Employ-ee's contri-bution
	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%
£50,000 –	23·2	1·1			45·2	1·5			20·4	0·3						
£40,000 –	25·2	2·4			26·2	2·9			25·6	2·5			26·4	2·5		
£35,000 –	53·0	2·2			30·0	1·7			22·8	2·2			24·5	2·5		
£30,000 –	27·7	3·4	13·0	5·0	36·8	3·5			25·7	2·7			23·8	1·4		
£25,000 –	32·2	4·4			23·0	3·3			25·7	2·5			19·1	1·4	12·0	8·0
£22,500 –	13·7	2·1	7·9	4·4	14·7	4·3	17·0	8·5	28·9	2·9			22·5	3·1	15·5	7·0
£20,000 –	25·4	3·1	8·3	4·7	18·9	4·4			27·5	2·2	18·0	9·0	21·8	3·3	16·8	8·1
£17,500 –	12·7	3·8	8·4	3·0	17·7	3·6	10·8	6·4	17·3	3·7	7·2	4·8	24·0	2·9	13·1	5·9
£15,000 –	17·5	4·8	9·8	5·2	17·7	3·9	9·8	5·4	15·5	4·1	12·1	6·4	25·1	2·9	13·2	6·7
£12,500 –	14·1	5·0	12·0	6·3	9·1	4·0	9·0	5·2	14·8	3·9	12·6	6·8	20·4	3·3	12·6	6·4
£10,000 –	13·0	6·0	10·8	6·0	14·7	2·4	12·1	6·3	15·6	4·9	13·2	7·2	16·9	3·5	12·5	6·4
£ 9,000 –	8·2	5·0							15·0	4·0			15·7	3·6	11·9	6·8
£ 8,000 –									15·2	5·0			14·7	4·4	12·5	5·7
£ 7,000 –									7·3	4·6	15·0	7·5	13·1	4·9	11·8	6·0
£ 6,000 –									8·8	4·4	16·0	8·0	11·6	4·7	11·8	6·0
£ 5,000 –													9·7	5·0		
Under £5,000													7·1	5·9		
Mean contribution	26·9	2·6	9·9	5·0	27·0	3·0	11·5	6·3	22·9	3·0	12·2	6·6	20·4	3·2	12·8	6·5
Number	*(103)*		*(42)*		*(132)*		*(31)*		*(763)*		*(42)*		*(1,685)*		*(401)*	

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(ii) and (iii), for this grade

E. A. JOHNSTON
GOVERNMENT ACTUARY

ANNEX I

VALUE OF SUPERANNUATION BENEFITS AS A PERCENTAGE OF SALARY THROUGHOUT CAREER

Table A—Values for top Civil Servants, senior officers of the Armed Forces, the Judiciary

(per cent of salary)

	Career leading to retirement in grade stated in table:		
	(Permanent Secretary)	(Deputy Secretary)	(Under Secretary)
Civil Service	24¼ (25½)	22¼ (22¾)	21¼
Career with similar final salary to civil servant with typical Nationalised Industry scheme benefits	23 (24)	21 (21½)	20
Career with similar final salary to civil servant with typical Private Sector company scheme benefits	19½ (20½)	18 (18½)	17
	(General)	(Lieutenant General)	(Major General)
Armed Forces	39¾ (41)	37½ (38)	36½
	(High Court Judge)	(Circuit Judge)	(Metropolitan Magistrate)
Judiciary	36 (36)	36 (36)	31

Figures in brackets are values calculated as if the salary levels recommended by the Review Body in 1974 had been implemented by 1977.

Table B—Values for senior posts in Nationalised Industries and in the Private Sector

(Taking into account the salaries in 1977 of the various posts)

(per cent of salary)

Category of Employer (by net assets in £ million)	Career leading to retirement as:			
	Chairman	Deputy Chairman	Other Board Member	Senior Executive
1. Nationalised Industries				
over 1250	24	23½	21½	21¼
over 250 but under 1250	23¼	22¼	22¼	21
over 50 but under 250	21	20¼	20¼	20¼
2. Private Sector Companies				
over 1250	39¾	37½	32¼	27¼
over 250 but under 1250	30¾	29½	26½	21
over 50 but under 250	25	24	20¾	18
over 10 but under 50	20¾	19¼	17¾	14¾
under 10	18¾	18¾	17	13¾
Financial Companies	29½	26½	26	21¾

Notes to Tables A and B:
1. These percentages apply to gross salaries, i.e. before deduction of superannuation contributions.
2. The assumptions made as to career length and age at retirement are described in the text.
3. The value of superannuation benefits shows the total contribution needed and includes any contribution payable by the employee.

CONFIDENTIAL

Prime Minister

JR

19/2

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

PRIME MINISTER

PUBLIC SERVICE PENSIONS

..... The attached note has been prepared at my request as a background to the discussions we are to have during the coming weeks on indexation of Public Service Pensions.

2. As you will see, we have made some fairly definite statements on the subject, which will doubtless be quoted if we attempt to change the system. But we are going to be caught in crossfire whatever happens, for the moves we are taking in other directions will only serve to underline the significance of the present advantage of public sector pensioners.

(G.H.)

18th February 1980

CONFIDENTIAL

CHANCELLOR

PUBLIC SERVICE PENSIONS

You asked me to draw together the various documents setting out the Conservative Party's position on indexation of public service pensions at and around the time of the 1979 General Election.

2. During the year preceding the General Election, Party opinion hardened in favour of some revision of the basis of calculation of public service pensions - most probably in the form of an increased deduction from pay - designed to ensure that the cost of index-linked pensions was properly covered. A copy of the guidance note then in use is attached.

3. The matter was not touched on in the 1979 General Election Manifesto.

4. Typical of the letters you were sending out was one to Mr Charles Messer of Newton Abbott, who had written to you asking about the Party's policy on public service pensions:-

> "The Conservative Party is not proposing to change the index-linking arrangement for existing public service pensioners. A real anxiety has, however, been expressed by the All-Party Public Accounts Committee about the extent to which the cost of this benefit, particularly at a time of high inflation, may be falling unfairly on the general body of taxpayers rather than upon those public service employees still at work who are to enjoy this particular benefit. We should, therefore, want to ensure that the deductions made from public sector pay cover the cost of index-linked pensions at a proper and realistic level."
>
> (19 April 1979)

5. The Party organisation set out a similar view in its General Election note "Questions of Policy 107 - 19 April 1979". A copy is attached.

6. On 23 April 1979 you were questioned in the course of a Robin Day Radio Four Phone-in programme by a Mr Morgan, of Nottingham. Mr Morgan recorded the discussion and his account was reprinted in the magazine "Civil Service Pensioner" published by the Civil Service Pensioners Alliance. A copy is attached.

7. This interview was quoted in a further General Election briefing note - "Questions of Policy No. 126, 24 April 1979" -

/Which

which took the form of answers to a questionnaire submitted by the Civil Service Pensioners Alliance. Copy also attached.

8. You were recently asked by Mr Jim Lester MP to comment on a letter which the same Mr Morgan had sent to him. A copy of your reply, which had been checked with No. 10, is attached. In this reply you indicated that there were circumstances in which index-linking of public sector pensions would be subject to intolerable strain.

9. I remind you also of the answer given by Mrs Thatcher under one of the headings in a questionnaire sent in by one of the ex-service organisations. This answer, prepared for Mrs Thatcher by Sir Ian Gilmour and Peter Joynes, was later quoted in the journal "Pennant", published by the Officers' Pension Society in November 1978:-

> Index Linking of Pensions
>
> "I can assure you that the Conservative Government will continue with the present arrangements."

Summary and conclusion

10. Throughout the run-up to the General Election, answers on this subject always emphasised the need to vary the deduction from civil servants' pay in order to ensure that the cost of their pensions was properly covered.

11. When it came to the actual index linking of pensions, you replied in one letter " . . . not proposing to change the index-linking arrangement for existing public service pensioners". (My emphasis.) In the Robin Day phone-in you went rather further in declaring that "there's no intention to do that" - i.e. "to take this benefit (index linking) away from public sector pensioners".

12. Public concern about the unfairness inherent in index linking of public service pensions has rumbled on since the election; it has tended to concentrate on the senior ranks of the civil service, and has fed on a number of stories about persons who have been retired a long time and whose indexed pensions have run ahead of the present salary rating of the job they were formerly doing.

/13. Any

13. Any proposal to break or modify index linking will meet with strong opposition from some of those affected. But a failure to act will draw strengthening criticism from the private sector - so long, that is, as inflation remains a dominant economic issue. The Government will have to weigh these considerations, and act in the context of current changes in the index-basis of other social security benefits and fiscal parameters.

P J CROPPER

15 February 1980

GUIDANCE NOTE 1978

From: The Rt. Hon. Sir Geoffrey Howe, QC MP

HOUSE OF COMMONS
LONDON SW1A 0AA

INFLATION PROOFED PENSIONS: A NOTE

The principle of automatic inflation-proofing for public sector pensions was established, after a debate which had stretched over many years, by the Pensions (Increase) Act 1971. At that time inflation was running at such a comparatively low rate that many private pension schemes were able to increase pensions more or less in line with inflation. In those circumstances it was generally argued that it would be right for public service pensions to receive similar treatment. Many other countries reached the same conclusion.

The position does, of course, look very different today because the Government have allowed inflation to reach such disastrous leve

This is the cause of our present anxiety. For although most public service pensioners receive quite modest pensions, their recent increases have certainly been larger, in percentage terms, than most private pension funds have been able to afford, and in many cases pensions (and some other benefits) have risen faster tha earnings.

People who have no pension, but only an investment income to live on, have particularly resented the fact that they have been paying higher taxes but receiving no increase in income. Some public service pensioners have themselves begun to question the justice of the position.

Even so there is substantial (and understandable) reluctance to break faith with existing pensioners by challenging the originally sensible general principle of the 1971 Act. The way to avoid that is for the Government to give over-riding priority to reducing the rate of inflation as far and as fast as possible.

It can, however, be argued that the pension contributions made by public servants do not take sufficient account of higher inflati rates - indeed the Government has admitted as much. This question cannot at present by examined by the Pay Research Unit, which has been suspended by the Government. But, as I expect you will have se from recent press reports, it is now being considered by the House of Commons Select Committee on Expenditure. The Expenditure Committ undertook a major investigation of the pay, conditions and manning the Civil Service early in 1976. It is expected to produce the most important report on the Civil Service since the Fulton Report of 19

We are awaiting the outcome of this investigation, and meantime concentrating our attack on the Government's failure to get inflati under control, which is the root cause of present problems.

PUBLIC SECTOR PENSIONS

Question

What will a Conservative Government do about inflation-proofed public sector pensions?

Suggested Answer

The principle of automatic inflation-proofing for certain public sector pensions was first established by the Conservative Government in the Pensions (Increase) Act of 1971. For private sector employees a considerable degree of inflation-proofing is now provided not only in the state retirement pension but also in the new second pension scheme, whether state or private. We are not therefore proposing to change the index linking provisions for public sector pensions.

There is, however, a real problem about the way contributions are assessed in the public as compared with the private sector. The cost of inflation-proofing to the taxpayer has risen substantially as a result of the sharp increase in the rate of inflation. This has given rise to a real sense of grievance amongst those working in the private sector, for whom complete inflation-proofing of occupational pensions is impossible and who feel they have to pay through taxes for the inflation-proofing of others. The most important remedy is, of course, to reduce the rate of inflation as fast as possible.

We would ensure that the independent Pay Research Board is fully satisfied that the deduction which is made from public sector wage settlements for index linked pensions is realistic.

Background Note

Pension contributions are natioanl and are not deducted from public employees' salaries. But their notional value is taken into account in determining fair relationships between public and private pay for comparable work.

Conservative Research Department,
24 Old Queen Street, London, SW1

19.4.79

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

24 January, 1980

Dear Jim

I thank you, belatedly I fear, for your letter of 13th December, enclosing one from your constituent, Mr. R. Morgan.

Mr. Morgan is quite right to remind me of the Radio 4 broadcast on 22nd April. Indeed, I remember my conversation with him perfectly clearly.

I have no wish to undermine the legitimate expectations of retired public servants; I was a loyal member of the Government which introduced the indexation legislation in 1971 and recognised the obligations then undertaken.

At the same time we have to recognise the strong feelings that are generated on this subject, among people who have suffered very acutely from the impact of inflation on fixed investment incomes and unindexed pensions.

Taking a hypothetical, but not entirely fanciful example, let us envisage a situation in which, one year, the Gross National Product fell 10 per cent and prices rose 20 per cent. In that combination of circumstances I am sure you would agree that full indexation of public service pensions would be almost impossible to sustain. Beyond a certain point, the protection of the real living standards of one particular part of the community at the expense of all others might force any government to reconsider its obligations.

It is, of course, up to all of us to try and prevent these circumstances being realised. The present Government is indeed

J. Lester, Esq., M.P.

straining every sinew to bring the rate of inflation down and prevent the international energy crisis from having too serious an impact on the domestic economy. If we are successful then the clamour for an end to indexed pensions will subside. Nobody would be happier, then, than I.

Meanwhile, the relative future cost of maintaining indexed public service pensions has grown considerably as a direct result of the past few years of inflation. You will know that, in relation to some public services, arrangements have been made to increase the notional deductions from salary which stand proxy for the employee contributions which are made to private funded schemes. The government is at present reviewing the basis of these arrangements and may well find it appropriate to seek further and wider adjustments in future.

GEOFFREY HOWE

Telephone :
Nottingham 256344

14 Beeston Fields Drive
Beeston
Nottingham
NG9 3DB

Hon Member for Beeston

9.12.79

Dear Mr. Lester,

I am aghast to read in today's Sunday Times that "Mr William Clark, Conservative MP for Croydon South and his influential finance committee of Conservative MP's" is calling for the suspension of the index-linking of public service pensions.

I was personally assured by Sir Geoffrey Howe in a Radio 4 broadcast on 22nd April 1979 that the Conservatives would not do this. 0905 a.m: Robin Day

In view of the importance of this pledge, I had its full text published in the Civil Service Pensioner Magazine I also retain the original tape-recording of this pledge in Sir Geoffrey's voice.

I cannot believe he will dishonour it and would welcome your re-assurance.

Please accept my congratulations on your ministerial appointment and also the season's greetings,

Sincerely,

Reginald Morgan

This is an extract from the Summer 1979 edition of the magazine 'Civil Service Pensioner'. The magazine is published by The Civil Service Pensioners' Alliance

GENERAL ELECTION PLEDGES

From Mr. Reginald Morgan of Nottingham

I was fortunate enough to get included in Robin Day's Election Call programme on Radio 4 on 22nd April 1979, and spoke to Sir Geoffrey Howe who is now Chancellor of the Exchequer. Had the result of the election gone the other way, there would have been no point in getting his statement into print, but now you may think it worth putting on record. Fortunately I tape-recorded the interview, so can give it verbatim. In addition to the following, I also asked about the State Retirement Pension indexation, but I believe this was subsequently well aired, so have not included it. The part relating to Public Service Pensions went as follows:

QUESTION. Although the Conservatives brought in the Pensions Increases Act of 1971, which index-linked public service pensions, many Tory backwoodsmen have since sniped at it. Do the Conservatives intend to take this benefit away from public service pensioners?

SIR GEOFFREY HOWE. No, there's no intention to do that, Mr. Morgan, and you're right to remind us that it was introduced with all-party support in 1971, because you may remember that for years before that, there had to be periodic protests on behalf of retired people, who had been Public Servants, to get any account taken of inflation in the level of their pensions. But of course it's important also to make sure that the cost of those benefits, which existing public servants are going to enjoy, is properly shared and the all-Party Expenditure Committee in the House of Commons a little time back, recommended that there should be an independent examination, to make sure that the contributions being made by those still in service, towards the value of the benefits they are going to get when they retire, should be properly assessed to make quite sure they really are paying the full value, as do of course people working for private organisations in contributory pension schemes.

...ted and root out waste. And I'll give you one illustration of why we think we can be successful at that, if you compare what's happened to the rates charged in London Boroughs this year, and of course waste can take place in local Government as well as in Central Government - in the Boroughs that are under Labour control rates have gone up by 26 per cent on average this year; in the Boroughs under Conservative control by 2.6 per cent. So that it does show that it's possible if one is firm, in tackling waste, for a Conservative administration to reduce it very substantially.

DAY:

Mrs. Collins thank you. Next Mr. Reginald Morgan in Beaston Nottinghamshire. Mr. Morgan it's your Election Call to Sir Geoffrey Howe.

MORGAN:

Thank you Mr. Day, good morning gentlemen. Although the Conservatives brought in the pensions increases Act of 1971 which index-linked public service Pensions, many Tory backwoodsmen have since sniped at it. Do the Conservatives intend to take this benefit away from public service pensioners?

HOWE:

No there's no intension to do that Mr. Morgan, and you're right to remind us that it was introduced with all-Party support in 1971. Because you may remember that for years before that there had to be periodic protests on behalf of retired people who'd been public servants to get any account taken of inflation, in their level of their pensions. But of cour[se] it's important also to make sure that the cost of those benefits which existing public servants are going to enjoy, is properly shared. And the all-Party expenditure Committee in the HOuse of Commons a little time back recommended that there should be an independent examination to make sure that the contributions being made by those still in service, towards the value of those benefits they're going to get when they retire, should be properly assess to make sure they really are paying the full value as do of course, people working for private organisations in contributory pension schemes.

DAY:

Mr. Morgan?

MORGAN:

Yes yes that's fair enough. This also has

CIVIL SERVICE PENSIONERS' ALLIANCE

Questionnaires from branches of the above body have been sent to candidates asking various questions. Because the questions vary a little, an answer in general terms, as under, is suggested. Specific questions that have been identified are dealt with individually in the Background Note below.

Suggested Answer

I have carefully studied the proposals which are mentioned in your letter. I have to point out that our Manifesto makes clear that control of inflation must be an overriding priority. It would be difficult to reconcile most of the proposals you put forward with that objective, which inevitably involves keeping down public expenditure. Our Party introduced the revised very generous Civil Service pensions are currently adjusted. Sir Geoffrey Howe has said (on 23rd April) when asked whether Conservatives intended to take this benefit away from public service pensioners: "No. There is no intention to do that". The question of raising the "ceiling" for old age income tax allowance is one for the future Conservative Chancellor of the Exchequer and I don't think one should anticipate his next budget proposals. I deal elsewhere with the question of concessionary fares /see Question 5 below/.

Background Note

Question 1

"Increases in Civil Service pensions, as for National Insurance pensions, should be based upon either the Retail Prices Index or the Earnings Index, whichever is more favourable at the time".

Civil Service pensions are based on the Retail Price Index under the Social Security Pensions Act 1975. Mrs. Thatcher has reaffirmed our commitment to increasing the level of retirement pensions "to take account of price rises. That is to say....in terms of what they will buy in the shops" (Gravesend, 17th April 1979).

Question 2

"Increases in Civil Service pensions should apply to those retiring from the Service before the age of 55".

The point about this question is that it is only on reaching retiring age that the pensioner who retires prematurely becomes eligible for an annual index-linked review of his or her pension. Effectively, within the Civil Service the provision for retiring on pension at 55 (or earlier on a reduced pension) only applies to prison officers. But outside there are many thousands to whom this concession would have to be offered - armed forces, police, MPs etc. For most of these it was the Conservatives who lowered the age-bar from its former level of 60 to 55. A further

24.4.79

concession could only be considered when economic curcumstances permit.

Question 3

"Civil Service earnings depressed by Incomes policies should be adjusted for pensions purposes".

It is a complaint of the Service that because incomes restraint was imposed on them more effectively than on private enterprise and because pensions are based on one's final year of earning, the level of pensions was kept artifically low for Civil Servants. Of course the same could be claimed for other enterprises that loyally observed wage-restraint policies. But candidates might feel justified in saying that the Conservative Party is concerned about this grievance and when returned to office would wish to assess its impact and extent with a view to some amelioration of the position.

Question 4

"The 'ceiling' for income tax allowances shpuld be abolished".

Old age allowance for income tax currently stops at £4,000 p.a. The future level of the 'ceiling' is a matter for general taxation policy.

Question 5

"A national scheme for concessionary bus fares for pensioners should be introduced".

Concessionary fares are covered in Questions of Policy : 63 (q.v.).

Question 6

"Widows of Civil Service Pensioners who retired before 1972 should receive half pension, instead of one-third".

Before 1972, when the Conservatives brought in the revised Civil Service pension scheme, Civil Servants paid actuarily calculated contributions to provide a one-third provision for widows. There is now an increased contribution to give widows a one-half pension.

Question 7

"Pensioners who are over the age of 80 years who are entitled to a non-contributory State pension should have their pensions made up to the normal State retirement pension".

After the 1966-70 Labour Government had refused to do anything for the over-80s, it was the Conservatives who introduced a special non-contributory pension for them. The over-80s have now been drawing this pension since 1970 (in some cases since 1971). Its rate is lower than the normal NI retirement pension because Retirement Pensioners will have paid contributions for many years - in many cases for all their working lives - whereas the over-80s will not. But the over 80s' pension is protected against price rises because it is linked to the level of the Retirement Pension, which we are pledged to increase "to take account of any price rises" (See Question 1 above).

Conservative Research Department,
24 Old Queen Street, London, SW1

24.4.79

with compliments

MINISTER OF STATE

CIVIL SERVICE DEPARTMENT
Whitehall London SW1A 2AZ

Telephone 01-273 5563/4086

Econ. Pol.

CONFIDENTIAL

Minister of State

Civil Service Department
Whitehall London SW1A 2AZ
Telephone 01-273 3000

7 February 1980

The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer
HM Treasury
Parliament Street
LONDON SW1P 3AG

R 7/2

Dear Geoffrey

INFLATION PROOFED PENSIONS

In his letter to you of 31 January, Norman Fowler refers in passing to a meeting which I had on 30 October with the Public Services Pensioners' Council. At that meeting I said that the Government had no plans at present for legislative change, but went on to say that no responsible Government could give categorical assurances that the present arrangements for inflation-proofing would never be changed in future. The Government would have to take account of the prevailing economic circumstances. The Council did not dispute this.

I am sending copies of this letter to Members of the Cabinet, Norman Fowler and Sir Robert Armstrong.

Y.
Paul

PAUL CHANNON

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-7 FEB 1980

Econ Pol.

Ref: A01335

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PRIME MINISTER

NBPM TL 2/2

Public Service Pensions: Index Linking

In his minute to you of 1st February the Chancellor of the Exchequer suggests that his officials, with help from the CSD and DHSS, should prepare a paper for E setting out the broad considerations bearing on, and possible legislative options for, breaking the index-linking of public service pensions. I am sure it is right that Ministers should take a hard look at this emotive area on the basis of the facts, in order to decide whether action should be taken. I think that you can welcome the Chancellor's proposal.

2. In doing so perhaps you should remind the Chancellor of the remit he obtained from E Committee on 23rd January to bring forward a further paper on his proposal to seek higher contributions from public service pensioners for the benefits they enjoy. The two proposals should be looked at together because they are alternatives. One can raise contributions or reduce benefits but hardly both.

3. I would also hope that the Treasury paper would be supported by an adequate factual analysis. I can say, without revealing the activities of previous Governments, that this is not a subject which has gone unresearched, in considerable depth, in recent years. As your colleagues discovered when E Committee discussed the Chancellor's "contributions" proposal, the complexities and ramifications can be very wide. Indeed it was for this reason that I suggested in my brief for the January meeting that there could well be a case, at the end of the day, for establishing some kind of independent inquiry - perhaps a Royal Commission - to take a fundamental look at pensions across the whole of the public sector.

4. If you agree your office might reply to the Chancellor on the lines of:-

(a) you welcome a paper of the kind he suggests as a basis for an early discussion in E;

(b) you would want it and the paper already commissioned on "contributions" to be looked at together;

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(c) you regard it as essential that both papers should not merely increase arguments but should also contain a factual base adequate for an informed discussion.

RA

Robert Armstrong

5th February 1980

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BK

File

Econ Pol

10 DOWNING STREET

From the Private Secretary

5 February 1980

The Prime Minister has read the Chancellor's minute of 1 February about the possibility of suspending the index link in respect of public service pensions. She agrees that Treasury officials should take the lead in preparing a paper on this subject which would then be taken in E Committee towards the end of this month.

I am sending copies of this letter to Don Brereton (Department of Health and Social Security), Geoffrey Green (Civil Service Department) and David Wright (Cabinet Office).

T. P. LANKESTER

John Wiggins, Esq.,
HM Treasury

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1

Prime Minister

Agree that Chancellor should submit a paper to E?

TL 4/2

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

PRIME MINISTER

PUBLIC SERVICE PENSIONS : INDEX LINKING

In the light of the Cabinet decisions on breaking the index link for a range of social security benefits, I think we need to look again at the indexation of public service pensions. We need to consider how we might take statutory power to suspend the link, whether for all public service pensioners or to some more limited extent. Ideally we should be in a position to take a decision on this for announcement at the same time as the social security package now agreed - and one possibility is indeed that we could legislate by way of an amendment to the Social Security Bill now in Committee.

2. This is a difficult area, and before we decide whether it can be tackled along these lines, I propose that my officials, with help from CSD and DHSS, should prepare a paper setting out the legislative options and the broad considerations which we should have in mind in reaching a decision. Their remit would be to consider, in particular, what form the legislation should take, what limitations might be put on the power to suspend the index link, and what categories of pensioners should be covered.

3. If you agree, I will ask my officials to take the lead in preparing this paper, which we might then consider in E Committee towards the end of this month.

4. I am sending copies of this to the Secretary of State for Social Services, Minister of State CSD, and Sir Robert Armstrong.

M. A. Hall

pp. GEOFFREY HOWE
1st February 1980

[Approved by the Chancellor of the Exchequer, and signed in his absence].

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2 - FEB 1980

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2

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

MINISTER OF TRANSPORT

The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer
Treasury
Parliament Street
LONDON
SW1

31 JAN 1980

Prime Minister
To glance

Dear Geoffrey.

INFLATION PROOFED PENSIONS

Thank you for sending me a copy of your recent minute to the Prime Minister on this subject. I have no objection to what is proposed so far as it concerns Civil Service pay, but there are two points which I should like to register in connection with nationalised industry pension schemes.

First, it would be advisable in any public announcement about this not to suggest that the recommendations of the proposed inquiry will be applied to self administered, funded, public sector pension schemes. Such schemes have a legal existence separate from that of the sponsoring industry, and are usually based on a trust deed. The current service contributions paid to these schemes are determined by the schemes themselves and it would seem inappropriate to seem to be questioning the adequacy of their decisions, particularly since, for current service, there is usually no guarantee by

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the industry or the Government that any deficiencies attributable to indexation will be made good.

Secondly, as you know, the Transport Bill, at present in Commons Committee, alters the means by which Government support is being provided for the historic pensions obligations of the British Railways Board. My proposals have been greeted with some suspicion by the Unions who are concerned (rightly or wrongly) that my new proposals do not provide the same degree of assurance of indexation of pensions that the previous funding scheme would have afforded. They see that under the Bill, the ending of indexation for Civil Service pensioners could mean the ending of indexation on the "historic" element of railway pensions, which might not have happened under the previous regime. In my consultations with the Unions, and during the second reading debate on the Bill, I have referred to the assurance which I understand Paul Channon recently gave to representatives of Civil Service pensioners that we have no present plans to end indexation of their pensions. While I am not suggesting that the particular problems of the Railway Pension Funds should inlfuence our consideration of the wider issue of indexation of public sector pensions, it is obviously very important that my Department be kept in touch with developments, since this could well become an issue when the Transport Bill Committee reaches the pensions clauses in the Bill.

I am sending copies of this letter to Members of the Cabinet, Paul Channon and Sir Robert Armstrong.

NORMAN FOWLER

cc HMT.

Original in G/R

Econ Pol

C.f. to note

10 DOWNING STREET

THE PRIME MINISTER

30 January 1980

Dear Sir Nicholas,

Thank you for your letter of 10 January and your kind remarks about my "Weekend World" appearance.

The question of indexed pensions is very much in my mind and, like you, I am troubled at the extent to which the rapid increase in inflation of recent years has created a growing disparity in the treatment of different pensioners, far beyond what was foreseen in the House of Commons when the legislation to index official pensions was first enacted. And, as the Department of Health and Social Security letter to the Secretary of your pension fund makes all too clear, the Government machine often shows inadequate appreciation of the problem.

Inflation is the root of this, as of so many other problems in our economy and society. If we can get inflation down, and keep it down - as we are determined to do - that will certainly be the best way of tackling the pensions problem. In a society without serious inflation, there would be strong arguments for trying to maintain the value of pensions during the years of retirement.

Meanwhile, the relative present and future cost of maintaining indexed public service pensions has certainly grown considerably, and I agree that it is questionable whether public service occupational pensioners should have their real living standards fully protected, when real living standards are falling for most of the rest of the population.

/One possible

One possible solution would be to withdraw or limit the indexation - this would be, as you suggest, a hard decision; it would also involve complex legislation, defining for the wide variety of public sector pension arrangements some appropriate alternative arrangement.

Another approach may be to ensure a more satisfactory charge on the employees concerned to reflect the full cost of inflation-proofing. We are at present reviewing the arrangements for determining these charges, and we may well decide that a bigger adjustment to employees' salaries is needed.

All best wishes.

Yours sincerely

Margaret Thatcher

Sir Nicholas Cayzer, Bt.

CONFIDENTIAL

D8

10 DOWNING STREET

From the Private Secretary

SIR KENNETH BERRILL

Actuarial Assumptions for Pension Funds

The Prime Minister was grateful for your note of 23 January in which you explain the point which you raised in E Committee. She assumes that the Treasury are taking this point on board in considering the question of public sector pensions further.

I am sending a copy of this minute to David Wright (Cabinet Office) and John Wiggins (HM Treasury).

T. P. LANKESTER

28 January 1980

CONFIDENTIAL

GC

Original in G/R

cc MOD
CSD
IG.
Const.

Econ Pol

CF to note

24 January, 1980.

Dear Julian,

Thank you for sending me the letter which you received from Mrs. B. Dent of 2 Lismoyne Close, Fleet, about the indexation of Armed Forces pensions.

I am sorry if the interview I gave to Weekend World on 6 January should have caused Mrs. Dent any concern. The discussion was concerned, at that point, mainly with the indexation of earnings, and with the indexation of short term National Insurance benefits payable to people normally in employment. My only reference to pensions was when I re-affirmed our pledge that old age pensions would keep pace with rising prices.

But the Government has to recognise that there is some public concern about the existing arrangements for inflation-proofing public service pensions. Since the introduction of these measures inflation has continued at a high level and as a result their cost has proved considerable. Moreover, many other pensioners are not protected against inflation to the same degree. The Government is, therefore, looking into this matter, but the issues involved are complex, and I can assure you that no decisions have yet been taken. Full account will, of course, be taken of the assurance which we gave to the

/Officers

Officers Pension Society in August 1978 about indexation of pensions. We do, however, believe that it is essential that pensions contributions paid by public servants are fair and seen to be fair by the public generally.

Yours ever,

(SGD) MT

Julian Critchley, Esq., M.P.

Original in G/R

c.c. CSD
Const.
Mr. Gow

CF to note

24 January, 1980.

Dear Elaine,

Thank you for your letter of 7 January enclosing one from your constituent Mr P L Stiles, proposing that public service pension increases should be related to salary movements for the groups in question, rather than to movements in prices.

As Mr Stiles says this is not a new idea. The case for "parity" as it is known, was pressed strongly by public service pensioner organisations at the time of the Pensions (Increase) Act 1971. It certainly has some theoretical attractions. It would, for example, have avoided "overtaking", whereby somebody who retired between 1976 and 1979, when pensionable salaries were depressed by the Labour Government's incomes policy, can receive a lower pension than a colleague retiring before or after that period.

The big drawback to parity, however, is its cost. Historically, earnings have normally increased faster than prices: the period of the last Government's incomes policy was exceptional in this respect. As a result the greater cost of parity in the long run has not been readily apparent over the last few years. But as real earnings begin to increase parity becomes more expensive than price protection. As you know, we have proposed in the Social Security Bill that the basic retirement pension should henceforth be linked to price movements rather than, as now, the higher of earnings and prices.

The Government are examining the inflation-proofing of public service pensions. In particular, if present arrangements for inflation-proofing are to continue, it is essential to ensure that pension contributions paid by public servants are fair and seen to be fair

/by

by the public generally. As Paul Channon told the House on 7 November, we believe there should be an independent scrutiny of the calculations on which Civil Service pension contributions are based. We are at present considering how this could best be achieved.

Yours ever,

(SGD) MT

Mrs E Kellett-Bowman MP

2

CONFIDENTIAL

Qa 04408

To: MR LANKESTER

From: SIR KENNETH BERRILL

Prime Minister

This repeats the point Ken Berrill made at E. No doubt the Chancellor will take into account.

TL 24/1

Actuarial Assumptions for Pension Funds

1. At E this morning I questioned that part of the possible remit of a Three Wise Men study on indexed pensions which included consideration of the assumptions used by the Government Actuary in his calculations on public sector indexed pension schemes.

2. By far the most important assumption is the likely yield in real terms of a pension fund's portfolio of assets over the thirty or so years ahead that an actuary needs to look. I believe that the 'classic' assumptions lie in the $2\frac{1}{2}$-$3\frac{1}{2}$ per cent range. Obviously it is very difficult in these inflationary/slow growth times to rely on anything better than 0 per cent, and the Three Wise Men might indeed argue for a very low figure. But for the Government to join them would mean agreeing that our present economic troubles had best be assumed to be incorrigible as far ahead as one can see - a position which would have some presentational problems.

3. But presentational problems apart: the results of the Government arguing for a very low rate of return could be serious if the assumptions were adopted for the whole public sector (as the Chancellor suggested in his paper) and if they became the norm in actuarial assumptions over private sector pension funds as well.

4. Lowering the assumed rate of return for an unfunded central government pension scheme (civil service, armed forces, NHS) means putting up the "employee's contribution" (i.e. deduction made in pay calculations) but there is no immediate effect/via the employer's contribution because in an unfunded scheme there is not one. But in funded schemes (private sector schemes and 2.9m. employees in the public sector - nationalised industries, local government employees, etc.) the employer traditionally puts in around £2 to the employee's £1. So any changed assumptions would be an immediate burden on private industry, nationalised industry prices, local authority rates, etc.

5. Also the proportion of the nation's savings flowing through pension funds would rise - perhaps sharply. The investment managers of pension funds are seldom to be congratulated for their imaginative appreciation of the nation's investment needs (especially in manufacturing); they are more often accused of holding Governments to ransom by refusing to buy gilts till the rate of interest has been raised.

6. Obviously the assumption of a very low real rate of return on assets 1980-2010 has advantages to the Government in terms of the salary calculations for armed forces, NHS and central civil servants. But the other possible effects are such that one needs to weigh them carefully before embarking on a Three Wise Men exercise which could get the Government into having to argue publicly that the new assumptions were better and hence deserve to be applied generally.

7. I am sending a copy of this minute to Martin Vile and Tony Battishill.

(Thany)

KB.

23 January 1980

NBPM
arrived too
late for E

PRIME ~~MINISTER~~

INFLATION PROOFED PENSIONS

T.
24/1

The Chancellor suggested to you that an independent body should be set up to fix, on the basis of material supplied by the Government Actuary, a broadly reasonable figure for the value of public sector inflation-proofed pensions. This would replace earlier proposals to put both Civil Service pensions and job security issues to the Pay Research Unit Board, which seem to have foundered on Staff Side opposition. My major direct concern is with the pension arrangements for the National Health Service, which also involve inflation-proofing. But from whichever aspect one approaches this problem, given the continuing criticism of inflation-proofed public sector pensions and the Cabinet's decision to try to meet this criticism by securing larger "contributions" than at present from the potential beneficiaries, some way forward must I think be found. In my view the Chancellor's proposals are well worth trying.

2. I can understand Jim Prior's misgivings about the public sector employees' reaction to a body composed on the lines the Chancellor suggested, but I think that we shall run into public sector union opposition to any arrangement for reviewing the value of inflation-proofed pensions. What is important is that the arrangement we propose should carry conviction with the public, and for that the presence of informed lay opinion, as well as a strictly actuarial view, seems essential.

3. I am copying this minute to members of the Cabinet and to Paul Channon.

PJ

23 January 1980

PJ

Original filed 4R

C.F. to note

cc HMTsy
DHSS
CSD
Ian Gow

10 DOWNING STREET

THE PRIME MINISTER

22 January 1980

Dear Peter,

Thank you for your letter of 19 December expressing particular concern about the economic effects of the present system of funding public sector pensions and with which you enclosed an interesting paper on pension funding. You wrote in similar terms to Geoffrey Howe. I am replying for both of us.

Your paper covers the problems associated with the financing of occupational pensions in both the public and private sectors. As the paper rightly points out, it is primarily for the private sector to make its own decisions about pensions provision. I therefore propose to confine any detailed comment to the effects of switching to pay-as-you-go in the public sector. However, before dealing with this specific question I would like to make a number of general points.

The present pattern of pensions provision in this and other countries is largely a matter of economic and social history. Thus, the Pay-as-you-go (PAYG) systems currently operated in France and Germany were introduced as a result of periods of catastrophically high levels of inflation which undermined totally these countries' ability to capitalise pension liabilities. (The current level of pension provision in France and Germany of course derives from the generally higher level of

/wages

wages and salaries which they are able to pay as a result of their superior post-war economic performance, rather than PAYG per se.) The British experience has been different. Admittedly we have seen in the last decade the development of a worrying gap between the yields on pension funds' assets and the rate of wage and price inflation. This has caused the present disparity between the pension benefits available in the public and private sectors and lies at the root of much of the concern expressed about inflation proofing of public service pensions. However, though these developments are worrying, they are in no way comparable with the devastating problems which led to the adoption of PAYG in other European countries. They certainly do not justify a wholesale switch from the present system of pension funding to PAYG, with all the attendant disruption which such a switch would entail.

This brings me to my second point. Pension funding involves taking a very long-term view of the growth of pension liabilities and the investment income and contributions required to finance that growth. There are almost bound to be periods when the liabilities will grow faster than the rate of return on invested funds. Provided, however, that these periods are not prolonged, or the gap between the growth in liabilities and assets does not become too large, this does not call into question the underlying rationale for funding. Here I would take issue with the figures which you quote about pension funds' performance over the last fifty years. Data on the performance of individual funds are not readily available (certainly not for the period back to 1929) but what evidence there is tends to suggest that up to 1970 the yields on the pension funds' main assets (equities and government stock) have on average exceeded or at least kept pace with the growth in final salaries. Moreover, even though the 1970s have not been a happy period from the point of view of pension fund performance, it is important not to exaggerate the impact of the poor returns on investment on the growth in

/contributions

contributions in recent years, which is as much a reflection of the increase in the general level of wages and the trend to scheme benefits linked to final salary schemes.

One final general remark: I agree with you that if the trend evident in the 1970s were to continue then the viability of the present system of funding occupational pensions would be threatened. But this would be only one, albeit serious, manifestation of the unsatisfactory performance of the British economy. The real solution lies in achieving a substantial improvement in our economic performance. I am bound to say that there is little to suggest that a general switch to PAYG would contribute significantly to the achievement of this vital goal as there is no evidence to indicate that the existence of funding or the need to make good deficiencies has in the past been the cause of lack of investment in productive industry.

I now turn to the specific question of the effects of switching public sector pension funds over to some system of PAYG. At the outset I can assure you that we have given very full consideration to the possible benefits to be derived from such a switch. Unfortunately, the economic impact would be minimal. The essential point is that switching to PAYG would not, as you imply, create additional resources but merely affect a redistribution of the pattern of income or financing. (This conclusion is unaffected by the existence of inflation-proofing for public sector pension schemes.) There would, I accept, be a substantial reduction in the Public Sector Borrowing Requirement. But this would be exactly matched by a reduction in the funds available for investment. The markets would thus quickly recognise this as purely a cosmetic move. More importantly, because pension funds invest only a proportion of their money in gilt-edged stock there would be a shift in the relative demand and supplies of different forms of securities. As the reduction in supply of financial assets would be concentrated on public sector securities, while the reduction in

/demand

demand would be spread between private and public sector liabilities, the result would be a reduction in interest rates on public sector securities relative to the yields on liabilities of the private sector. The price of equities would therefore be depressed making it more difficult and expensive for the private sector to raise new capital. This would run counter to the basic thrust of our policies which are aimed at re-ordering the public sector's affairs so they place less of a burden on the private sector.

There is another important consideration in respect of those public sector bodies, such as the nationalised industries, whose activities involve a significant element of trading and which are competing with the private sector. In these cases the existence of some system of funding pension liabilities ensures that the public sector is competing on all fours with the private sector and that decisions about employment reflect the full costs of employing labour at the time at which they are incurred.

You will gather from what I have said above that we do not consider that there is a case for the wholesale switching of funded public sector pension schemes over to a system of PAYG. I would, however, add that I share the concern expressed in your paper about the growing concentration of assets in the hands of institutional investors, such as pension funds. As you are no doubt aware, there has been a very considerable volume of evidence submitted to the Wilson Committee on this subject and we shall therefore be looking forward with considerable interest to what the Committee's Final Report will have to say on this. Whatever the outcome of these deliberations I must stress that we do see valuable economic and social benefits from encouraging the widest possible participation by individuals in the ownership of real and financial assets. The declining trend in personal shareholdings is therefore worrying. The substantial cuts in direct taxation announced in the Budget are

/but a

but a first step in restoring personal incentives to save and build capital, We recognise that further measures will need to be taken if the present trends are to be modified.

Yours ever

Peter Hordern, MP.

Econ Pol

CONFIDENTIAL

Ref. A01204

PRIME MINISTER

Inflation-Proofed Occupational Pensions

(E(80) 4)

BACKGROUND

When E (not Cabinet as the Chancellor's paper says) discussed inflation-proofed occupational pensions on 15th January they took no decisions but asked the Chancellor to explain his proposals in more detail and, as an aid to thought, to include also draft terms of reference for the "wise men". It was clear that most colleagues saw considerable political difficulty in tackling inflation-proofing as such, and were attracted by the Chancellor's suggestion that attention should be concentrated on increasing the contribution which staff make to the cost of their pensions.

2. The problem in the Civil Service is that there are elaborate arrangements, built into the basic pay agreements, for determining the value of Civil Service pensions and comparing them with the value of pensions paid to the analogues used as the basis of "fair comparisons". These arrangements involve actuarial calculations by the Government Actuary, and both sides are in effect committed to honour the result of his calculations. The course of the discussion then, and indeed the Chancellor's paper now, sought to avoid this complication by arguing that the "right" to index-linking had a "subjective" value above that within the scope of the Government Actuary's arithmetic, and that a monetary value could properly be set on this for the purpose of pay negotiations. The suggestion of the "wise men" was designed to provide a mechanism by which this subjective element could be valued.

3. The terms of reference proposed by the Chancellor, and annexed to his paper, cover this point in (b). They also add, at (a), a review of the assumptions and methods used by the Government Actuary in assessing the value of <u>full</u> inflation-proofing in public sector pensions and the <u>60 per cent</u> inflation-proofing achieved on average in the private sector analogue schemes.

They also include, at (c), a request to the "wise men" to consider how to assess, also for pay negotiation purposes, the value to staff of the higher job security attaching to public sector work.

4. The essential questions for Ministers are:-

(a) Whether they accept that index-linking of public sector pensions as such is politically untouchable, and that attention should therefore be concentrated on contributions. If so, a willingness to say this at a suitable point would help the saleability of the general proposition to the employees concerned.

(b) Whether they accept the form and membership of the inquiry as suggested in paragraph 10 of the Chancellor's paper.

(c) Whether they accept the proposed terms of reference. It would be as well here to consider each of the three elements in turn. Thus:-

Rate of real return on assets

(i) The Government Actuary's assumptions and methods.

1:2 The advantage of the Actuary agreeing to use tougher assumptions would be that the results would carry through automatically into Civil Service pay under the terms of the pay agreements. But the Government Actuary is a professional, doing a professional job, and the Inquiry will need to walk delicately, given especially that it is, as proposed, a non-expert body.

(ii) The value of the guarantee. This is the central object of the exercise and on the face of it could yield useful results. But the Civil Service unions are likely to argue that they have no real guarantee of index linkage - being dependent on the whim of Parliament - and, if asked to pay, could well ask, as a quid pro quo, for the guarantee to be strengthened. If there is no real prospect of going back on inflation-proofing - and Governments of both Parties have been aware of the difficulty of doing so - then strengthening the guarantee might not in reality be a high price to pay. The Committee could usefully ask the Chancellor and the Civil Service Department, in parallel with the present operation, to consider what form an improved guarantee might take (e.g. could it be written into contracts of service?).

(iii) Job security. Assessment here could well require a good deal of research because the concept of placing a value on job security is unfamiliar. The Committee will want to be clear whether they are asking the "wise men" to suggest methods of assessment or whether they are seeking an early view on monetary value. The former is compatible with a quick operation - because the bulk of the work will be left to be done by someone else at a later stage - but the latter is not, especially if the results are liable to be challenged at arbitration, as they certainly would be if disadvantageous to the staff.

(d) Whether they accept the view in paragraph 12 of the Chancellor's paper that even the limited task for the "wise men" is probably too much to be tackled in time for this year's Civil Service pay negotiations (which effectively start in February) and should therefore be seen as a lead-in to subsequent negotiations either with the non-industrial Civil Service next year or with other parts of the public service this year.

(e) Whether, if there is now more time, they would prefer to consider a more fundamental examination of the problems than that envisaged by the "wise men" - perhaps by way of a Royal Commission.

HANDLING

5. You will want to ask the Chancellor to introduce his paper and then have the views of the Secretary of State for Employment (who saw the Chancellor's paper in draft and does not dissent from it) and the Minister of State, Civil Service Department before opening the discussion more widely.

CONCLUSIONS

6. You will want to record conclusions on:-

(i) Whether the Government is prepared to say that it accepts the continuation of index-linking for public service pensions and proposes to concentrate on getting adequate payment (or deduction from pay) for them from staff in service;

(ii) the membership of the new group;

(iii) the terms of reference of the new group.

7. If the Committee now preferred a more wide-ranging inquiry - perhaps by way of a Royal Commission, you would need to invite the Chancellor, in consultation with the Secretary of State for Employment and the Minister of State, Civil Service Department, to produce specific proposals.

RtA

(Robert Armstrong)

22nd January, 1980

MASTER

CONFIDENTIAL

Only copy - please file & mark grid

NOTE

The circulation of this minute has been restricted. Recipients are accordingly asked to ensure that the secrecy of its contents and the need to know principle is strictly observed.

CONFIDENTIAL

P.0190

PRIME MINISTER

INFLATION-PROOFED PENSIONS

(Minutes to you from the Chancellor of the Exchequer dated 10 January and from the Minister of State, Civil Service Department dated 11 January)

BACKGROUND

see Econ Pol (Pub Ex) Pt 7

When the Cabinet discussed public expenditure on 13 December 1979 (CC(79) 25th Conclusions, Minute 6) a good deal of attention focussed on the malign effect of the Retail Price Index (RPI) on public expenditure generally. Although no conclusions were reached there was a widespread view that all index-linked expenditure, including social security benefits and public sector pensions, ought to be looked at again. However, in the discussion the Chancellor indicated, and he had discussed this view with you before the meeting, that attention on public sector pensions might more fruitfully be concentrated on the contributions made by employees rather than by seeking to remove index-linking as such. Following this thought his minute to you of 10 January suggests that, in order to get results usable in this spring's pay negotiations with the non-industrial Civil Service, there should be a quick and subjective review by a small group of people of distinction, authority and experience who would be asked to establish a principle to be used in evaluating inflation-proofed pensions in public sector pay negotiations. By way of illustration he suggests a group comprising Lord Boyd-Carpenter, Alex Jarrett (Chairman of Reed International and an ex-Civil Servant) and R E Holland (Chief General Manager of Pearl Assurance). In his minute of 11 January Mr Channon supports this approach.

2. I understand that the Secretary of State for Employment* is likely also to concur with the Chancellor's general proposition though he will have points to make about the membership of any group and will want to return to the

*Minute of 14 January now received

in the folder

R.

parallel problem of evaluating job security (which is currently being looked at in general terms by the Clegg Commission).

3. This area is of course a political minefield because, while index-linked pensions give rise to a good deal of criticism, they are enjoyed as a statutory right by large numbers of public employees ($5\frac{1}{2}$ million of them, according to the Lord President's memorandum of 26 October last to E Committee (E(79) 60)) and are seen by them as a protection against the employer depressing the real value of his pension commitments. Apart from the large number of public sector employees involved it is relevant also that all state retirement pensions are index-linked as is the earnings-related supplement which enables all non "contracted-out" employees to build up a higher pension entitlement under the national scheme. Most of the working population, therefore, have a direct interest in the principle of index-linking. Moreover, as the Chancellor pointed out in Cabinet, the public sector beneficiaries include "emotive" groups like nurses and members of the armed forces. And they also include many of the most articulate members of society. It was no doubt this consideration which led the Chancellor to prefer to tackle the contributions rather than the pensions end of this particular equation.

4. Your colleagues may or may not want to take a decision now on whether they accept the principle of index-linked pensions as such - and thus concentrate wholly on the adequacy of contributions - or whether they prefer to keep all their options open. Even if they feel that political realism points to the former course, however, they may nevertheless see advantage in keeping options open for the time being as a pressure point when negotiating higher contributions from Government employees.

5. However that might be, the Chancellor's minute is concerned with contributions and must be judged in that light. It has two weaknesses:-

a. The objective of the inquiry as described in paragraph 2 is "to establish a principle which is capable of being adapted to the variety of different [public sector] cases" which should then be "applied as widely as possible". But in paragraph 8 the inquiry is seen as "applying its subjective judgement and stating, without any pretence at precise mathematical accuracy, a broadly reasonable figure to reflect value". These objectives are not necessarily compatible.

b. It is short of facts, in a situation where these can constrain Government action.

6. If the inquiry is to be asked to advise on principles it risks being an unguided missile. Thus an obvious principle might be that the contributions of staff to their pensions should adequately and consistently reflect the value to them of those pensions. But there are wide differences within present public sector pension schemes in the value for money which contributors obtain. I understand, for example, that the Armed Forces Pay Review Body reflects pension rights in its awards by broadly following Civil Service practice. But because they are paid at an earlier age, armed forces' pensions have a significantly higher total value than do Civil Service pensions. The effect of this principle might therefore be that the contribution to be exacted from the armed forces, and possibly the police, to reflect pension rights would be considerably higher than at present.

7. An inquiry directed to principle could well suggest that, for clarity, Civil Service pay rates should be struck before, not after, allowing for the value of pensions and payment made for pensions by the staff from current earnings. Such an arrangement would reflect current private sector, and some public sector, practice and would have presentational advantages. It would however lead to a substantial once for all increase in the Government's apparent pay bill - an outcome which the Chancellor might not welcome. It would also raise questions about the size of the Government's own contribution to the pensions of its employees (at present thought by the CSD to be roughly on a par with private sector practice - at about 10 per cent of the wages bill) and might lead to pressure for the establishment of a pensions fund. This need not be an unwelcome development in itself but could have substantial implications in the Chancellor's field.

8. Given the wide disparity between staff contributions to pensions in the public sector (see Annex A to E(79) 60) it is unlikely that the inquiry would

be able to come up with a subjective valuation of index-linking as such - and indeed to do so would run into precisely those problems of professional competence to which the Chancellor draws attention in paragraph 9 of his minute. There is however one element of the value of index-linking which could be susceptible to value judgements - the value of the "guarantee" as opposed to the "best endeavours" basis of many private sector schemes. But even here there are snags: the staff could argue that, as no Government can bind its successor and Parliament is free to change the law, the "guarantee" is less solid than it appears; and the present pay agreement with the non-industrial Civil Service requires the value of pensions to be actuarially calculated and the staff have the right to go to arbitration (subject only to a Government veto on grounds of "policy") if they do not like the deduction proposed. In the case of teachers, of course, the veto can only be exercised by joint resolution of both Houses of Parliament.

9. The Committee will come to its own view but, given the complexities of public sector pensions generally it is arguable that quick and easy solutions are not available. The alternative would be to launch a full-scale inquiry either in-house as a preliminary to further decisions or externally through a Royal Commission or a Select Committee. Any such inquiry would however preclude action being taken in time to influence the pay negotiations, or Review Body reports, due this spring.

HANDLING

10. You will want to ask the Chancellor of the Exchequer to introduce the subject and then call for contributions from the Minister of State, Civil Service Department and the Secretary of State for Employment. You might then, I suggest, seek to direct the Committee's attention to four questions:-

a. Do they accept that index-linked pensions in the public sector should be retained and attention concentrated on ensuring that staff contribute adequately to the cost of the pensions?

b. Is the Chancellor's suggested quick inquiry an adequate response to the problem?

If so

c. /what membership would they wish to see and what guidance can be given on drafting the terms of reference?

d. If not do they favour a major inquiry and if so in what form?

CONCLUSIONS

11. Very much subject to discussion, the conclusions of the meeting might be:-

i. [That the Committee accept that the principle of index-linked public sector pensions will have to be retained] and immediate attention concentrated on the size of the contributions made by staff; and <u>either</u>

ii. that the proposals made in the Chancellor's minute of 10 January should be accepted and the Chancellor invited to consult further with colleagues on membership and terms or reference ; <u>or</u>

iii. that the Chancellor be invited to bring forward proposals for a wide-ranging inquiry by [a Royal Commission] [a Select Committee of the House] into public sector pension schemes generally; <u>or</u>

iv. to invite the Chancellor to commission an 'in-house' study of public sector pension schemes and the implications of change as a preliminary to further consideration of the issues by the Committee.

P Le CHEMINANT

Cabinet Office
14 January 1980

PRIME MINISTER

INFLATION-PROOFED PENSIONS

1 The Chancellor sent me a copy of his minute to you about this.

2 I agree that the Clegg Commission is not the right body to tackle the sort of enquiry proposed.

3 On membership of the enquiry, I think we must avoid giving the appearance of a group dominated by private sector management. There would be no chance of such a body commanding the confidence of the public sector employees (and perhaps some of the public sector employers) who will be affected, and the difficulties of getting the sort of figure the inquiry recommends actually applied in negotiations would be multiplied. I realise that the names the Chancellor mentions in para 9 of the minute are only for illustration, but as they stand I think this objection would apply. Lord Boyd-Carpenter would be seen as a private sector employer, since he has now retired from the Civil Aviation Authority but retains chairmanships and directorships in the private sector, and the other two names fall into the same category. I think we must face the fact that if the enquiry is to command confidence as an impartial exercise, a representative of the trade union view is needed.

4 For similar reasons I think we should consider whether to add on a representative of public sector employers - for example, an able Chief Executive from a local authority. It may be that 5 members instead of 3 would not be too many.

5 It is also essential to ensure that the group is fully able to subject the actuarial calculations and assumptions of the Government Actuary to informed and critical scrutiny. If there is to be no professional actuary on the group, it must clearly be

enabled to obtain - and if necessary pay for - the best available independent actuarial advice.

6 My last point arises on para 12 of the Chancellor's minute. As I understand it, the proposed group would be asked to set a broadly reasonable figure to reflect the value of inflation-proofed pensions. Clearly that would replace our earlier proposal to put the pensions issue to the Pay Research Unit Board. But it is not immediately clear how it could be held to replace the idea of putting the job security issue to the Board. We have asked the Clegg Commission to look at this question, and perhaps that is all that should be done. But if we can ourselves find no way of seeking to quantify the value of job security, we shall not be able to complain if the Commission finds itself unable to do so.

7 I am copying this to recipients of the Chancellor's minute.

J P

14 January 1980

PRIME MINISTER

INFLATION-PROOFED PENSIONS

I support the proposals in the Chancellor of the Exchequer's recent minute that a small and authoritative group of people should be asked to assess the value of inflation-proofed pensions. If the benefits are to remain, it is essential that all those who receive them in the public sector should pay the proper price - and be seen to do so.

As far as the Civil Service is concerned, I agree that this would replace the earlier proposal of a reference to the Pay Research Unit Board. When I met the National Staff Side yesterday they confirmed their objection to such a reference as being outside the Board's terms of reference. They also expressed concern about the reports in the press that the Government might make an arbitrary pay deduction in respect of inflation-proofing. They would regard this as a breach of the Civil Service pay agreement, as indeed it would be.

I agree with the Chancellor that we should not appoint to the group a practising professional Actuary in view of the possible difficulties in relation to the Government Actuary, who will certainly be one of the people the group will need to see.

I am sending copies of this minute to members of the Cabinet and Sir Robert Armstrong.

PAUL CHANNON

11 January 1980

P.C.

Prime Minister

This approach seems very sensible. The value of an index-linked pension must be a very subjective judgement, and not something just amenable to actuarial assessment. Mr Channon seems to be content - you might like to confirm this with him tomorrow. Assuming he is content, agree?

TL 10/1

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

PRIME MINISTER

INFLATION-PROOFED PENSIONS

Our discussion in Cabinet before Christmas led us away from ideas of limiting or removing the benefit of inflation-proofing of public sector occupational pensions, and towards adequate (larger than at present) "contributions" from potential beneficiaries.

2. There has grown up a wide range of contributions or salary abatements in different parts of the public sector in respect of pensions benefits which are all inflation-proofed, resting on a variety of past agreements and negotiations. There can be no single and simple way of dealing with them all. What I think we could aim to do, however, is to establish a principle which is capable of being adapted to the variety of different cases, and then see that it is applied as widely as possible.

3. Attempts at objective valuation of inflation-proofed pensions - of the kind which have in recent years been made for the non-industrial civil service by the Government Actuary - are widely believed to be inadequate. They involve contentious assumptions about long-term future developments of prices, earnings and rates of return on investment, and they cannot reflect the subjective value of security enjoyed by the beneficiary of full inflation-proofing. The problem - which is in some respects similar to the problem of evaluating job security - inevitably involves subjective judgement.

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4. To get at this we shall need a new breakthrough. If we are to affect 1980 settlements, we shall need it quickly - some of the most important public service groups operate, like the non-industrial Civil Service, on April settlements. It will not be easy.

5. One approach might be simply to try to negotiate an adjustment for the Civil Service and other major groups. But I think this would be weak. We would have no authority for the attempt other than our unilateral assertion; we would have to tackle the problem quite separately for each negotiation, with the risk of different outcomes, or ending up with the lowest common factor.

6. It seems to me, therefore, that we have to look for some outside judgment. The question is whether we can find a sufficient outside authority, and one which could do the work in time. I do not think we could ask the Clegg Commission to tackle this - their style would involve prolonged factual enquiry and taking of evidence, and an additional task would cut across their already tight timetable for handling references on teachers. I wondered whether there might be any possibility of using the House of Commons Select Committee which looked into the subject some time ago (in the previous Parliament); but I suspect that they also would feel the need to undertake a prolonged enquiry.

7. I have concluded - with reluctance and rather to my own surprise - that our best hope may lie in trying to find some new group of people - hopefully of distinction, of authority and of experience - whose considered opinion would be likely to command acceptance among reasonable people. They would have to be chosen and appointed specially for this purpose.

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8. It remains a question whether the task could be carried out without a heavy or prolonged burden of work, which must be avoided if it is to be done within a month or so. In principle, I believe it should be possible. There would be need for some inspection of evidence - actual levels of benefits achieved under private sector pension schemes and actual levels of contributions or notional salary reductions. Fortunately, material of this kind should be available from the current work being done by the Government Actuary. The task of the group would essentially be that of applying its subjective judgment and stating, without any pretence at precise mathematical accuracy, a broadly reasonable figure to reflect value. The terms of reference would need to make clear that the advice was needed quickly, and that it was judgment, rather than searching analysis, which was needed.

9. As regards membership, the short time-scale suggests that we need not be debarred from approaching people who have busy jobs already. We would need a lay chairman, at least one acceptable active business representative, and it would be useful to have somebody from the pensions/insurance industry. (I think we should avoid a professional actuary in that capacity, because of the difficulties that might create in relations with the Government Actuary.) As an illustration, a well-balanced trio could be: Lord Boyd-Carpenter, Alex Jarratt (Chairman of Reed International) and R.E. Holland (Chief General Manager of Pearl Assurance).

10. I cannot be certain that an approach on these lines would work. But I can see no other way of getting at a significant effect on the forthcoming 1980 public service settlements in time. Even getting the judgment from the right group of people could be difficult. Having got it, we would still face the task of making it apply in the various negotiations, but I would hope that we could expect some public support for doing so and, if we were able to launch the

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CHANCELLOR OF THE EXCHEQUER

process successfully in one or two negotiations, it would become progressively easier to extend it across the whole public sector. A good deal of money is potentially involved. One per cent on the non-industrial Civil Service pay bill would be over £30 million; but there are many other large blocks of public sector staff - about ten times the number involved in the nominal Civil Service - who should also be affected sooner or later.

11. I should add that I have not given up entirely the thought of de-indexation of the pension benefits themselves. I am satisfied that the outcome of our discussion before Christmas was right for the time being. But if efforts to get a more satisfactory "payment" for the benefits of inflation-proofing fail, I believe we would need to look again at de-indexation. This is a consideration which could be brought in to the discussion during negotiation with unions and staff associations in the light of any helpful recommendation from the kind of outside group I am proposing.

12. I believe that Paul Channon agrees that it would be sensible to try the course I have suggested. This would, of course, replace for the Civil Service our earlier proposal to put the pensions and job security issues to the Pay Research Unit Board (which seems to have foundered on Staff Side opposition). If you share our view, he and I will arrange to put to you considered terms of reference and a list of possible names.

13. I am copying this to other members of Cabinet and to Paul Channon.

G.H.

(G.H.)

January 1980

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