C(80) 50

29 July 1980

COPY NO 36

CABINET

PAY, PENSIONS AND ALLOWANCES OF MEMBERS OF PARLIAMENT

Note by the Secretary of the Cabinet

I attach a note by officials prepared in accordance with my instructions from Cabinet last week to arrange for officials to examine and report on the financial implications of the Motion on Parliamentary Pay, Pensions and Allowances passed by the House on 21 July (CC(80) 30th Conclusions, Minute 2).

Signed ROBERT ARMSTRONG

Cabinet Office

29 July 1980

PAY, PENSIONS AND ALLOWANCES OF MEMBERS OF PARLIAMENT

Note by Officials

INTRODUCTION

1. On 21 July the House of Commons amended the Government's motion on the pay and allowances of Members of Parliament in 4 significant ways: by providing that MP's pensions should be based on the rates of pay recommended by the Top Salaries Review Body (TSRB) as appropriate from 13 June 1980; by providing that the rate of accrual of MP's pensions should be 1/40th of pensionable pay for each year of service; by providing that MP's pay should "correspond with .... the salary paid to a specified grade in the public service"; and by providing that the secretarial allowance available to MPs should be raised to £8,000 a year from 13 June 1980. (The text of the motion as amended is at Annex A.) The Cabinet in its preliminary discussion of these proposals on 24 July (CC(80) 30th Conclusions - Minute 2) asked to be provided with further factual information before coming to a decision. This note fulfils that remit. It has been prepared by officials of the Treasury, the Civil Service Department (CSD), the Inland Revenue and the Government Actuary's Department under Cabinet Office Chairmanship.

THE SALARY BASE FOR MP'S PENSIONS

2. The current salary of MPs is £11,750 a year (the new rate for 1980-81 just accepted by the House). The Government had proposed that pensions in 1980-81 should be based on a notional salary of £13,150. The amended motion raises this notional salary to £13,750. If present conventions were followed MPs would pay their 6 per cent pension contributions on the full notional salary of £13,750, but would be credited with the difference between the contribution on actual salary of £11,750 and notional salary of £13,750 (ie £120 a year). As the Government motion before amendment offered such reimbursement on the extra contribution required for a notional salary of £13,150, (£84 a year), the area for manoeuvre is the extra contribution (£36 a year) on the higher notional salary of £13,750. In addition the Exchequer also contributes to the Parliamentary Pension Fund its 16 per cent share of the difference between notional and real salary. The relevant contribution on the extra £600 of notional salary would be £96 per Member, giving a total Exchequer cost of about £132 per Member or some £80,000 in all.

3. Ministers wanted to consider the possibility of making MP's pay for the additional concession on notional pay. We are advised that it would be ultra vires to make MP's pay the Exchequer contribution, as employer, to the cost of the additional notional salary. The question therefore is simply whether MP's might be asked to pay an extra £36 a head in 1980-81. Whether further extra payments would be needed in future years would depend on whether notional pay remained ahead of actual pay. Although the sum is small, MP's would be likely to resist such a proposal - and their acquiescence on a free vote is necessary. They would be likely to point to precedent (their notional salary has been ahead of actual salary since 1975 and the Exchequer has borne the whole cost of the additional cover); and to the fact that - as they will see it - the TSRB recommended rate of pay is theirs by right and that, by accepting staging, they are in effect already making an extra contribution of £2000 a head to the Exchequer in 1980-81.

4. In considering these matters Ministers will also wish to bear in mind that, because of the bunching of MP's retirements (voluntary or forced) at the dates of general elections, the real concern of MP's is with the size of their salaries (real or notional) in the twelve months preceding each election. MP's will be concerned therefore to preserve the concept of notional pay if they think this will give a higher pension entitlement than actual pay constrained by monetary targets, and to minimise their contributions in the interim. Assuming that the next election will occur in 1983 or 1984, the critical years from the point of view of MP's pensions will be 1981-82 and 1982-83. Whether there will be a difference between notional and actual pay in these years depends on the decision the Government will have to take next spring when the next TSRB report on MP's pay will be available, and on the decisions on linkage (and especially the salary base from which linkage applies) which will have been made before then.

5. It is obviously impossible to forecast what recommendations the TSRB might make next year. But if they were simply to add 9 per cent to their current assessment of the appropriate salary of £13,750, MP's pay would rise to £15,000 (an increase of 27 per cent over current rates). It must be regarded as likely therefore that the question of establishing a notional rate of pay for pension purposes for MP's higher than the rates actually in payment will continue for some years.

6. In addition to the direct costs of the concession on notional pay for which MPs have voted, there is also likely to be an indirect cost. As many members of the Cabinet recognised last week, a concession to MPs carries a strong moral obligation to make a similar concession to the other TSRB groups affected by the decisions to reduce pay below the TSRB recommended rates as well as for the senior PRU grades (Assistant Secretaries, etc) to whom arbitration was refused. About 8000 public servants had their pension entitlements reduced by these decisions. In the normal course of events over 1000 of these can be expected to retire or die before 1 April 1982 (the period during which decisions on notional pay in 1980-81 affect their pensions). This would cost about £1½m a year in 1980-81 and 1981-82, £600,000 in 1982-83 with a diminishing commitment thereafter. These figures assume in the case of Assistant Secretaries, Senior Principals and analogous grades that the relevant level of "notional" pay would be the rates offered by the CSD earlier this year before the decision was taken to refuse arbitration. The way in which this procedure would work is described in Annex B.

THE RATE OF PENSION ACCRUAL

7. The pension arrangements governing pensions throughout the public services vary from group to group (the main features of the existing schemes are described in Annex C.) The most important of the public service pension schemes - in terms of numbers of beneficiaries - are those relating to the Civil Service (700,000 employees), the National Health Service (700,000 employees) and local government including teachers (1,800,000 employees). These schemes are to all intents and purposes identical. Each is based on the accumulation of pension rights at the rate of 1/80th of final salary for each year of service with a maximum pension of half final salary. In addition each provides for a lump sum to be paid on retirement accumulated at the rate of 3/80th of final salary for each year of service. Actuarially there is little difference in benefit between these schemes and the MP's pension scheme. The lump sum for civil servants, nurses, etc equates broadly to the extra maximum pension of 16⅔ per cent of final pay which MPs are allowed to earn. And MPs have the right to commute a part of their pension to a lump sum.

8. The amendment proposes that MP's pensions should accrue at a rate of 1/40th of salary per year of service, compared to the existing rate of 1/60. This would not alter the maximum pension (of $\frac{2}{3}$ final salary) but would determine how quickly that maximum was reached. A full pension would be earned after $26\frac{2}{3}$ years service - and any longer service, either in the House, or outside it, (since pension rights can be transferred into and out of the Parliamentary scheme) would not add to pension entitlement.

9. Although MP's pensions are governed by a statutory scheme, and thus strictly outside Revenue 'approval', they have always been operated as if the Revenue limits applied ie subject to a maximum pension entitlement of two-thirds of final salary and employee's contributions limited to 15 per cent of salary. Under these rules a scheme providing for employee contributions in excess of 15 per cent is not approved and hence loses all entitlement to tax relief.

10. The terms of the amended resolution appear to require that all years of service by MPs, past as well as future, shall qualify for pension at the rate of 1/40th of final salary. If, as the Cabinet envisaged, the whole cost of the improvement were to be met by increases in the contributions of MPs from current salary, the rate of contribution initially would on average have to be about 33 per cent. If the Revenue rules were applied - and they do not have to apply to a statutory scheme - none of this contribution would attract tax relief. It can be assumed that an arrangement of this kind would not be acceptable to MPs.

11. An alternative arrangement might be to provide that only future service qualified for accrual of pension by 1/40ths. But even here, and again assuming that the whole cost is borne by the Member concerned, the contribution would be likely to exceed the 15 per cent limit even before allowing for any additional contributions which may be recommended by the Scott Committee as a valuation for the "certainty" of index-linked pensions. The same consideration would be likely to rule out allowing MPs to choose between remaining with the present 1/60th scheme, and paying extra for a 1/40th scheme for future service.

12. The barriers to any variant of the 1/40 scheme described above would of course disappear if the additional cost were borne by the Exchequer not by the individual MP. The Exchequer already contribute 16 per cent of salary (of which 7 per cent is a deficiency payment to cover the back service credit granted in 1965 and 1978 as against the member's 6 per cent. But if the Exchequer met the cost of this further concession (an immediate direct cost of £1.4m a year) widespread pressure could be expected from all other public service employees for equivalent treatment and this could be very expensive. For example the average Civil Service pensioner has only 27 years of qualifying service for pension so that actual Civil Service pensions average one-third rather than one half of final salary. Accrual at the rate of 1/53 for each year of service (the equivalent of 1/40th for MP's) would increase the average size of public service pensions by about a half - at an ultimate cost, assuming no retrospection, possibly in excess of £1 billion a year at 1980 values.

13. Faced with these arguments MPs will assert that the particular conditions of their employment mean that they cannot build up an equivalent pension to other public servants. They will point to the fact that the average life in the House of an MP is around 20 years rather than the 40 needed to acquire a full pension. This argument ignores the fact that MPs can for the most part earn pensions in other employment many of which will be transferable into the Parliamentary scheme. They will also argue that police, firemen and members of the armed forces can accrue pensions at a faster rate than they can (30 years for full pension in the case of a policeman). But very special considerations apply to these pensions - ie the physical demands of the job and hence the obligation to retire early - which do not apply to MPs.

14. But the real argument against a change in the rate of accrual of MP's pensions, however brought about, is that it is unnecessary. The arrangements which already exist for the purchase of added years, by periodic contributions, and the arrangements which existed from January 1979 to January 1980 for the purchase of added years by lump sum, enable MPs, within limits, to determine their own rate of accrual of pension rights. There will of course be individual cases where the Revenue rules, and the length of service by the MP, will result in a pension well below the maximum entitlement. But most MPs disadvantaged in

this way will have pension rights acquired outside Parliament. In any case it is unnecessary to change the structure of the scheme to cater for hard cases. But if a concession would be helpful, the easiest, and perhaps the most practicable, would be to revive the arrangements applicable last year for the purchase of added years by lump sum, which operated up to January this year. No other alternative seems viable unless the Exchequer contribution were increased significantly above its present level.

LINKAGE

15. If the pay of MPs is to be linked to some external indicator that indicator needs to be chosen. The options (considered more fully in Annex D) are -

a. Linkage to an index. We assume that Ministers will not want to pursue this option.

b. Linkage to one or more comparators in the private sector. Apart from the difficulty in choosing the comparators a private sector link could well, in present circumstances, give a relatively high result.

c. Linkage to a specific Civil Service grade: apart from the difficulty of choosing the most appropriate grade there would be a danger that if the Government chose a particular grade, eg Principal, the House of Commons might substitute a more senior grade. Control of MP's pay could thereby slip from Ministers' grasp.

d. Linkage to the rate of change in the pay of a single Civil Service grade or a group of grades: such a linkage - analogous to that already operated for setting the pay of prison officers - would avoid these problems but would require a decision to be taken on the appropriate starting pay from which linking would operate. The choices for starting pay are: the salary actually in payment (£11,750) which would mean abandoning the third stage payment to MPs, due next year; the rate of £13,150 recommended by the Government as the appropriate third stage payment in 1980-81; the TSRB recommended rate appropriate to 13 June 1980 (£13,750); or the rate determined next April by the TSRB as appropriate then.

SECRETARIAL ALLOWANCE

16. The House of Commons also voted to increase their office, secretarial and research allowance to £7,859 for the year ending 31 March 1981 and £8,000 for any subsequent year. The extra annual cost of the amended motion would be approximately £400,000 in total. In earlier discussion the Cabinet appeared ready to accept this change.

PROCEDURE

17. Ministers may find it helpful to be reminded of the procedural steps necessary to give effect to any or all of the points covered by the Commons Motions of 21 July.

18. The Motions passed by the House were advisory. The Motion dealing with pay, including the rate of pay for pensions purposes, needs to be followed by a substantive Motion carrying the Queen's Recommendation. This would deal with the actual salary to be paid from 13 June 1980 (£11,750) and from 13 June 1981 (£13,150). It would also make provision for the notional rate of pay (£13,750) for pensions purposes on and after 13 June 1980 and for the crediting to MPs of a sum to offset the cost to them of paying their 6 per cent pensions contribution and the difference between their actual and notional salary for pensions purposes. Such a Motion cannot be passed if amended from the form proposed by the Government. If amendments are carried the Queen's Recommendation needs to be sought again. No further decision is needed to deal with "linkage" which is simply an administrative means at arriving at recommendations to be put to the House in future, nor is a further Motion needed to give effect to the increase in Secretarial allowance for which the House voted. Provision for a revised accrual rate for MPs pensions would have to be sought in specific legislation.

19. It so happens that the form of the Motion passed on July 21 was defective in respect of the reinbursement to MPs of their pension contributions on notional salary. Although the House amended the notional salary figure from £13,150 to £13,750 they omitted to increase the relative offsetting credit from £84 to £120. It would be normal for the Government to put right such technical points in presenting a substantive Motion carrying the Queen's Recommendation. But if Ministers were to decide that Members should be asked to bear the cost of their pensions contribution on the extra £600 on notional salary they voted for themselves it would be possible, though no doubt highly unpopular, to tell them that as regards notional pay and reimbursement they were being given precisely what they asked for.

CONCLUSIONS

20. If an announcement of the Government's reaction to the Motion passed by the House of Commons on 21 July is to be presented before the recess, the Cabinet needs to take the following decisions -

a. Whether to attempt to face down the House of Commons and refuse to implement any of the concessions which the House has set as the price for accepting a 9.6 per cent increase in salary this year;

If this course is not acceptable, then -

b. Whether to accept that the pension entitlement of Members of Parliament in the year from 13 June 1980 should be based on a notional pay of £13,750;

c. If so, whether to seek to recover from MPs the £36 reimbursement which would normally be made to them in respect of the £600 by which the notional salary of £13,750 exceeds that of £13,150 which the Government has already offered.

d. Whether to extend the concession on notional salary to the other TSRB groups and to the PRU grades refused arbitration in respect of this year's pay settlement;

e. Whether to stick to the proposition that any new improvement in the accrual rate of MP's pensions should be wholly financed by the MPs concerned in the knowledge that this condition severely limits what can be done, probably to a new arrangement for buying added years by lump sum. If on the other hand Ministers are prepared to see an increase in Exchequer funding for improved accrual rates the precise nature of any scheme will need to be considered further.

f. Whether to accept that in future the rate of change in MP's pay should be linked with that of a suitable "basket" of Civil Service rates of pay - supplemented if necessary by infrequent TSRB reviews (at the end or beginning of each Parliament), rather than to a single grade, an index or private sector analogues.

CONFIDENTIAL

g. In the event that linkage is accepted, to decide the starting salary to which linking should apply;

h. Whether secretarial allowances should be improved as the House has asked;

i. The timing and content of any announcement of the Government's decisions.

Cabinet Office
29 July 1980

CONFIDENTIAL

That, in the opinion of this House, the following provisions about salaries and pensions of Members of this House should be made:—

(1) The salary payable to Members of each of the descriptions in the first column of the following Table—

(a) in respect of service on and after 13th June 1980 and before 13th June 1981 shall be at the yearly rate specified in relation to that description in the second column of that Table; and

(b) in respect of service on and after 13th June 1981 shall be at the yearly rate specified in relation to that description in the third column of that Table.

TABLE

Description of Member	*Yearly rate of salary from 13th June 1980 to 12th June 1981*	*Yearly rate of salary from 13th June 1981*
	£	£
1. Member not within paragraph 2.	11,750	13,150
2. Member or Officer of this House receiving a salary under the Ministerial and Other Salaries Act 1975 or a pension under section 26 of the Parliamentary and Other Pensions Act 1972.	6,930	7,670

(2) The ordinary salary of every Member in respect of service on and after 13th June 1980 shall be regarded for pension purposes as being at the rate of £13,750.

(3) Any Member, except one in whose case no deduction is required to be made under section 3 or 4 of the Act of 1972, shall be credited by way of supplement to his salary payable in respect of service on or after 13th June 1980 and before 13th June 1981, with amounts at the yearly rate of £84.

(4) In the light of the continued difficulty in providing fairly for the salaries of Members of this House, the salaries of Members should be regulated to correspond with the amounts of the salary paid to a specified grade in the Public Service.

(5) The annual amount of the pension payable to an honourable Member shall be a sum equal to the aggregate of the following amounts, that is to say—

(a) an amount equal to one-fortieth of the relevant terminal salary multiplied by the number of complete years comprised in his aggregate period of reckonable service as a Member, and

(b) an amount bearing the same proportion to one-fortieth of the relevant terminal salary as the number of days comprised in that period after the end of the last complete year comprised in it bears to three hundred and sixty-five.'.

That, in the opinion of this House—

(a) the limit on the allowance payable to a Member of this House in respect of the aggregate expenses incurred by him for his parliamentary duties as general office expenses, on secretarial assistance and on research assistance should be £7,859 for the year ending 31st March 1981 and £8,000 for any subsequent year; and

(b) provision should be made to enable each Member in receipt of the allowance to contribute sums, not exceeding in the year ending 31st March 1981 £786 and in any subsequent year £800, to an approved pension scheme for the provision of pensions or other benefits for or in respect of persons in the payment of whose salaries such expenses are incurred by him.

MEMBERS' SECRETARIAL WINDING-UP ALLOWANCE

That, in the opinion of this House,—

(a) provision should be made under arrangements approved by Mr. Speaker for an allowance to be made towards defraying the expenses of secretarial or research assistance which, after a person has ceased to be a Member of this House, is still required in connection with his Parliamentary duties; and

(b) the limit on that allowance should be one-sixth of the amount which, for the year in which that person ceases to be a Member, is the limit on the allowance payable to a Member of this House in respect of the aggregate expenses incurred by him for his Parliamentary duties as general office expenses, on secretarial assistance and on research assistance; and

(c) the allowance should be paid to the person who has ceased to be a Member or, if he has died, to his personal representatives or a person nominated by him or selected under the arrangements approved by Mr. Speaker.—[*Mr. St. John-Stevas.*]

ANNEX B

NOTIONAL PAY FOR OTHER TSRB AND SENIOR PRU GROUPS

If the Government decide to accept the views of the House on pensionable pay and agree as a consequence that the other TSRB groups should be given a similar benefit, then the following action would need to be taken. For all groups except Ministers the new level of pensionable pay would have to be promulgated as the proper rate for the job with effect from 1 April 1980, superceding any previously promulgated rates. This would only require appropriate letters and memoranda to be sent by officials but presumably the Government would wish to announce their decision in general terms when the statement on MPs' pay and pensions are made. At the same time it would need to be made clear that the Government could not commit itself to implementing the new rates (except for pension purposes) by any particular date and the actual rates in payment would be those announced by the Prime Minister on 7 July. For the TSRB groups the pensionable salary would be the full TSRB recommended rates. For Assistant Secretaries and Senior Principals the pensionable salary would be the formal offer which CSD would have made to the Unions had the Government not decided on a reduction (£22,000 and £18,000 for the respective maxima of the two grades) and it would be imposed by administrative action.

To increase the pensionable pay of Ministers a new Order-in-Council would be required. There would be timing problems in getting this Order through Parliament before the recess.

THE PARLIAMENTARY PENSION SCHEME AND OTHER PUBLIC SERVICE SCHEMES

1. All public service pension schemes, including the Parliamentary scheme, offer broadly the same benefits. The basic benefit is a maximum pension of $\frac{2}{3}$ final salary, up to a quarter of which the scheme member may opt to commute to a lump sum. The maximum permissible commutation is to a lump sum of up to $1\frac{1}{2}$ times final salary, reducing the continuing pension to $\frac{1}{2}$ rather than $\frac{2}{3}$ final salary. In the Civil Service, local government, NHS, armed forces and teachers' schemes, full commutation is automatic; in the Parliamentary and police and fire schemes it is optional. The judicial scheme gives an automatic lump sum of twice the annual pension, the lower ratio reflecting the highly favourable accrual rate.

2. The schemes are similar in other respects. All offer a half-rate widows' pension (although the Parliamentary scheme is the only one to offer an automatic half pension to dependent widowers) and smaller pensions to dependent children. Pension rights are fully transferable between all the schemes. In most schemes there is provision for purchasing added years of service, with the scheme member bearing the full cost. This was introduced for MPs by the Parliamentary Pensions (Purchase of Added Years) Order 1978, under which MPs may opt at any time to buy added years by periodical payments (deductions from salary). MPs may also opt, within 12 months of entering the House to purchase added years by a once-for-all lump sum payment; the 1978 Order also gave this option to all serving Members, lapsing in January 1980.

3. A further feature of the Parliamentary scheme is that when it was introduced in 1964, serving MPs were allowed to reckon service before that date, up to a maximum of 10 years. This maximum was increased in 1978 to 15 years for MPs still serving at that time. The cost of this concession is being met by the Exchequer through annual deficiency payments into the Fund.

4. In most schemes, including the Parliamentary scheme, the full pension accrues over 40 years. Certain schemes offer more rapid accrual. Prison officers, policemen, firemen and the armed forces normally have to retire earlier than other groups, because of the requirement for physical fitness, and the fast accrual rate reflects this. The very rapid accrual rate for the judiciary is largely historical, going back to the 1920s and beyond: its original purpose was to compensate judges for the inability to earn any pension in their previous employment at the Bar.

5. The table on the next page summarises the accrual rates for the main public service schemes, and the contributions paid by the employee.

Length of time over which full pension accrues	Scheme	Number of members	Employee contribution (% of salary)
15 years (20 in some cases)	Judiciary		
30 years (1)	Police Fire Prison Officers (2)	127,000 38,000 20,000	7% (men), 5% (women) $6\frac{3}{4}$% $8\frac{1}{2}$%
34 years (from age 21) 37 years (from age 18)	Armed Forces Officers Armed Forces other ranks	37,000 276,000	(3) not quantified
40 years	MPs Civil Servants Local Government NHS Teachers	635 685,000 1,098,000) 728,000) 662,000	6% $8\frac{1}{2}$% (5) 5% (manual) 6% (non-manual 6%

Notes:

1. Police, fire and prison officer pensions accrue at the rate of 1/60th for the first 20 years of service and 1/30th (ie double accrual) for the next 10, up to a maximum of 30.

2. Prison officers belong to the Civil Service scheme and their pay is set by reference to the pay of other civil servants. Consequently, they pay the same average contribution.

3. Non-contributory scheme. The AFPRB allow for the value of pension benefits, but do not publish figures for any adjustment. Expenditure on armed forces pensions is about 25% of that on pay.

4. Excluding prison officers.

5. The Civil Service scheme is non-contributory, but pay research salaries are reduced to take account of pensions. If the scheme were contributory, male civil servants would pay $8\frac{1}{2}$%.

LINKAGE

The House of Commons have voted in favour of MPs' pay being "regulated to correspond with the amounts of the salary paid to a specified grade in the Public Service".

If the Government accepts the views of the House on linkage, there will be no need to reach immediate conclusions on the nature of the link. The House could be told that the Government agreed to the principle of a link and would bring forward detailed proposals for the consideration of Members in due course. However Ministers may wish to have the following points in mind when making their decision in principle:

Type of link: The link could be a direct one, so that MPs' pay would correspond exactly with the actual rate of pay of a particular grade (or the average of the rates of several grades); or it could be indirect, so that MPs' pay would increase by the same percentage as the pay of the specified grade or grades without necessarily being at the same level. The former option poses much more severe problems of finding suitable analogues. As it is generally accepted that the work of MPs is like that of no other group, any direct link would be open to question. With an indirect link the starting level for MPs' pay would need to be fixed: the obvious choices are the updated third stage (13,150), the rate of pensionable pay voted by the House (£13,750) if this is accepted by the Government, or an entirely new rate, perhaps based on a further report by the Review Body.

Number of analogues: MPs pay could be linked with a single grade, as envisaged in the Commons amendment, a group of grades, or a general indicator such as the Department of Employment's New Earnings Survey which the Review Body's thirteenth report felt was the least objectionable form of linkage. A link with a single grade would have serious disadvantages. It might be difficult to find a grade on which the House and the Government could agree, and the sensitivity over Members' pay would be transferred to the linked grade. A link with a general indicator would smack of indexation.

If the link were with a group of grades, the components of the group would need to be chosen carefully. It would be administratively simpler and less likely to produce freak results if all the grades were within the Civil Service but even a broad link of this sort could be sensitive with, for example, the Civil Service unions.

Periodic Reviews: Even if MPs' pay were linked, it would seem appropriate for it to be subject to an independent review periodically, perhaps once every five years or at the beginning or end of each Parliament. The review would need to consider whether MPs pay was still at the right level after several years of linkage and perhaps also whether the nature of the link was satisfactory. The review could presumably be done by the Top Salaries Review Body.