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Prime Minister

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*We discussed this with G-10
and decided to hold the announcement
until we have for the names of
all the members of the enquiry.
Otherwise agreed
ad.*

Dr T

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 had
the Chancellor
to announce
when he has
ask the members
lined up.*

[Handwritten signature]

[Handwritten signature]
M A HALL
Private Secretary

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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 against the background of national economic and social considerations.

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