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CABINET

CIVIL SERVICE CASH LIMITS: PAY AND MANPOWER

Memorandum by the Minister of State, Civil Service Department

1. It is now essential to settle the size of the global cash limit for the pay of the non-industrial and industrial Civil Service so that negotiations with the non-industrials, whose pay date is 1 April, can begin, and also to fit in with the general Estimates timetable.
2. To take this decision, we have to consider:
 - a. the overall size of the pay award to be made to non-industrial civil servants from 1 April, and the contingent provision to be made for the industrial pay settlement from 1 July; and
 - b. the size of a compensating volume squeeze.
3. The Chancellor of the Exchequer's report from the Ministerial Group on Cash Limits and Civil Service Pay (MISC 38) sets out some of the main options.

CASH LIMITS

4. Cabinet decided on 13 December (CC(79) 25th Conclusions, Minute 7) that the provision for pay and price increases in public sector cash limits, other than those for Civil Service and Armed Forces pay, should be 14 per cent.
5. The Chancellor of the Exchequer proposes in his latest paper (C(80) 14) that cash limits should be unchanged. I am assuming in this paper that Cabinet will endorse his proposals. If cash limits in other fields were to change, then the situation on Civil Service pay might be very different.

PAY RESEARCH EVIDENCE

6. The major part of the Pay Research Unit's evidence which, under the terms of the Civil Service Pay Agreement, should serve as the basis for this year's non-industrial settlement has now been received and examined by my officials. The Government Actuary has decided that the deduction for pensions should be increased from 2.6 per cent to 3.8 per cent. By application of the most stringent criteria, the average level of increase in pay rates indicated by pay research is reduced to around $18\frac{3}{4}$ per cent. Every effort will be made in the course of negotiations to reduce this figure, but it is the lowest we could defend, if necessary at arbitration, as consistent with the Pay Agreement.

7. The Annex to this note describes the background. As it makes clear, the unions have the right to go to arbitration. Breaking the Pay Agreement could only be effective if we were to withdraw that right.

THE PROBLEM

8. If the cash limit for Civil Service pay were to provide for pay increases of $18\frac{3}{4}$ per cent there would be a gap of just over 4 percentage points (ie, the equivalent of $4\frac{3}{4}$ per cent on the Estimates provision increased by 14 per cent) as compared with the generality of other public service cash limits. This is a big difference and we need to consider how we can narrow it.

THE OPTIONS

9. There are a number of options open to us. The two extremes are:
- a. to decide on a cash limit which finances fully a pay research settlement of $18\frac{3}{4}$ per cent; and
 - b. to restrict the Civil Service pay settlement to a 14 per cent increase if that is the provision for cost increases made in public service cash limits generally.

10. I believe that we should reject both these options, the first because it would be politically and financially unacceptable; and the second because of the grave consequences for industrial relations and hence the operation of Government. We should have to expect the collapse of all order and restraint in Civil Service pay negotiations. We should, unlike any previous Government, have enlisted behind the militants the great bulk of the loyal staff.

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11. We must therefore look for an intermediate way of bridging the gap. The Chancellor of the Exchequer's memorandum (C(80) 16) suggests a combination of a manpower squeeze and a staging of the implementation of the pay settlement.

STAGING

12. When I saw the Staff Side recently they stressed their determination that the Government should honour the Pay Agreement, i.e. that the full amounts due should be paid from 1 April next. They asked me to let my colleagues know the strength of their feeling. They feel strongly about staging as well as about the actual amount resulting from the pay research exercise. It was dissatisfaction about staging that led to last year's troubles.

13. Staging would be a breach of the Agreement and would require denial of the right to arbitration on the timing, but not the amount, of the increase. A modest degree of staging might not in itself cause the widespread industrial action to be expected from an imposed cut on the size of the increase but if it were taken beyond the limits discussed in the next paragraph we should risk industrial action, in which management grades are likely to join, on a much larger and more damaging scale than hitherto experienced. My colleagues can judge better than I what that might mean for their operations.

14. We must consider the permutations in the Chancellor of the Exchequer's paper (C(80) 16) against this background. The unions are likely to accept, however grudgingly, whatever degree of manpower squeeze we consider feasible if it is part of a successful attempt to avoid breaking the Pay Agreement. But the other possibilities of reducing the pay cost are very limited. It might be possible to shade the increase down to, say, 18 per cent if, with a manpower squeeze, that enabled us to honour the Pay Agreement, in particular to avoid staging. If we have to consider going beyond that, my judgment is that a negotiated settlement consistent with the Pay Agreement will be beyond reach. In that situation our best prospect of avoiding industrial action on a major scale will be to go for a modest amount of staging. We should be inviting much worse trouble if we were to attack the amount of the increase itself.

A SQUEEZE ON MANPOWER

15. It follows therefore that we should go for the largest practicable squeeze on manpower. If nothing is done, our planned growth in manpower in 1980-81 virtually cancels out the savings already agreed. There will be no significant reduction next year in Civil Service numbers. That will be quite unacceptable to our supporters. On industrial relations grounds, also, I believe a squeeze will be the least damaging of a number of difficult courses.

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16. Above all, I do ask my colleagues to consider the political effect of announcing an $18\frac{3}{4}$ per cent pay increase for the Civil Service, with only a 1 per cent reduction in manpower. Are we to see the British Steel Corporation lay off steelworkers in South Wales and British Leyland thousands of car workers in the Midlands but to say that the size of our own Departments can be reduced by only 1 per cent? So the outcome would be:

- a. pay increase of $18\frac{3}{4}$ per cent;
- b. some degree of staging;
- c. a 1 per cent manpower squeeze;
- d. index-linked pensions to continue though with increased contributions.

I find this package totally unacceptable politically. Unless we take stronger steps on manpower we shall infuriate our supporters without even avoiding the prospect of industrial action to boot.

17. I am well aware that a further squeeze on manpower will not be easy, but there is an annual turnover of more than 10 per cent in Civil Service staff. I do urge my colleagues to look at the wider interests of the Government as a whole and the need to have a package that we can all defend publicly. In spite of all the difficulties I do not believe we have exhausted the possibilities for dropping work. For all these reasons I propose that we do the same as last year, ie. have a further 3 per cent squeeze with the same limited exemptions as before. Time simply does not permit a more sophisticated course.

A RECRUITMENT BAN

18. To achieve savings in staff costs of 3 per cent in a single year will call for determined measures, and colleagues will wish to consider whether we should reinforce the cash squeeze by a general ban on recruitment, as we did last year. A ban would have the advantage of bringing numbers - and hence costs - down quickly and thus of reducing the size of the rundown required from a more gradual approach. On the other hand, last year's experience showed a ban to be a blunt and not altogether effective instrument. It was haphazard in incidence; it was often disruptive of efficiency; Ministers authorised exemptions to the extent of about 50 per cent of normal recruitment in order to recruit staff they considered essential. A further ban this year would be likely to do long-term damage to the ability of the Civil Service to recruit the people that on any reckoning we are going to need. If it is the only way to ensure that we strike our target, we should not flinch from it, but the scope for exemptions will need to be much more

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rigorously confined. My colleagues will wish to consider whether we should adopt this course, and, if so, what the timing and duration of the ban should be.

REVIEW OF THE PAY RESEARCH SYSTEM

19. There is certainly a case for a fundamental review of the pay research system. But if we still want an agreed and structured system which imposes discipline on unions negotiators and fosters good industrial relations we must accept that:

- a. there is virtually no possibility of negotiating with the unions a different system which would meet these requirements, especially if the point of departure was unilateral breach by the Government of the present agreement;
- b. it would probably need the authority of a major enquiry both to do justice to the subject and to secure the parties' acceptance of a new system;
- c. We should need workable interim arrangements in the meantime.

20. There is no need to decide this issue today, and I suggest I should put a paper to my colleagues very shortly.

CONCLUSION

21. Of the options canvassed by the Chancellor of the Exchequer, a 1 per cent squeeze on manpower would offer no hope of a negotiated settlement; only with a 3 per cent squeeze would I have any real degree of confidence that a negotiated settlement might be possible. There are also wider implications I have covered in my paper. I therefore conclude:

- a. that we should go for a 3 per cent squeeze on manpower and a 1 per cent reduction on pay, preferably by negotiation but otherwise by imposed staging;
- b. that I should be authorised to negotiate pay settlements for the non-industrial Civil Service on the basis of a.;
- c. that I should put a further paper to my colleagues on the future of the pay research system.

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Civil Service Department

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PAY - IN CONFIDENCECivil Service Pay ArrangementsThe Pay Agreements

1. The pay of the non-industrial Civil Service (about 550,000 staff) is determined on the basis of fair comparison with the pay of outside employees engaged on broadly comparable work, taking account of differences in conditions of service. Pay research in accordance with this principle has operated since 1955 but the detailed methodology has been developed and improved. The current Pay Agreements date from 1974 and 1977.

2. The 1974 Agreement provides for an annual pay research settlement to be paid in full from 1 April each year. It also prescribes in detail how the evidence collected by the independent Pay Research Unit is to be processed by management and unions to arrive at new pay rates for the Civil Service. The 1974 Agreement continues in force subject to the right of either side to give 6 months notice of withdrawal from all or part of it.

3. In 1977 as a condition for the re-activation of pay research for 1979 a new Agreement complementary to the 1974 Agreement provided various measures to strengthen the independence of the system. In particular it established the Pay Research Unit Board (Chairman: Lord Shepherd Vice-Chairman: Sir Derek Rayner) to oversee the work of the Unit and to ensure its integrity and independence.

London Weighting

4. Since 1974 London weighting has been determined, in common with many other public sector bodies, by use of the formula devised by the Pay Board. This is based on average extra costs incurred by those working in London and requires the use of special price indices from the Department of Employment which are published in June. London weighting is normally reviewed annually with effect from 1 April.

Arbitration

5. The unions have access to arbitration under the terms of the Civil Service Arbitration Agreements on all aspects of the operation of the pay research system and the fixing of London weighting. They can take cases to arbitration unilaterally on disputes up to and including Principal level. Successive Governments have nonetheless reserved the right to restrict access to arbitration on grounds of national policy, but this right has been used very sparingly.

Estimating the results of Pay Research

6. The final date for the Pay Research Unit to update its reports is 7 February. There are over 600 reports each giving in detail the pay and conditions of service of a number of specific jobs found by the Unit in an outside organisation to be analogous to the Civil Service grade in question. By applying the detailed rules of the Pay Agreements an adjusted pay rate can be calculated. The reports have been analysed in the most stringent way, and wherever there was any doubt about the interpretation of the evidence the lowest figure has been used. For each grade the negotiations centre on the median of the adjusted pay rates. Because pay research is based on detailed job-for-job comparisons the median pay rates which result reflect the outside market rates for each type of work covered. The percentage increases indicated for each grade can thus vary considerably from each other. The estimate of 18.75% is an average of these rates for different grades and thus represents the lowest possible figure which could, if challenged, be defended as being consistent with the Pay Agreements. Although every effort would be made in the course of negotiations to reduce this figure, the actual outcome of negotiations would depend critically on the attitude of the unions and on whether they wished to take matters as far as arbitration.

Industrial Civil Service

7. There are no formal pay or arbitration agreements for the industrial Civil Service. Their pay has however been determined on a broad basis of comparability for very many years.

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A comparability study is in hand but there is no formal commitment that its results will be implemented in this year's settlement. In the estimate it has been assumed that an increase will be indicated of similar size to that for the non-industrials.

Cost of a Pay Research Settlement

The provision being made in the 1980-81 Estimates for civil service pay (including London Weighting and employers' national insurance contributions) is about £4100m. A settlement of 18 $\frac{3}{4}$ % for non-industrial staff would add about £635m to the pay bill. This includes the estimated cost of London Weighting. If there were to be a settlement of the same size for industrial staff, this would cost a further £95m. The cash limit will include also provision for pay increases for staff in the Northern Ireland Civil Service and in certain fringe bodies whose pay is linked with that of the civil service. This will add some £50m to the size of the cash limit, making about £780m in all.