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SECRET

P.0267

PRIME MINISTER

PUBLIC SECTOR PAY

(E(80) 46, 47, 48 and 49)

BACKGROUND

You will recall that you held an ad hoc discussion on public sector pay issues with a number of your colleagues on 19 May. The Chancellor's paper (E(80) 46) discharges the remit he was then given. In addition you have a Note by the CPRS (E(80) 49) commenting on the Chancellor's paper; a paper from the Lord President of the Council (E(80) 48) on Civil Service Pay; and a further Note by the Chancellor (E(80) 47), prepared jointly with the Paymaster General and Bernard Ingham, suggesting a campaign of public education about pay. Taken together these papers represent a formidable range of ideas about a formidable and complex subject. You will want to decide as discussion progresses whether, and if so which, decisions can be taken at this meeting. Obviously the more ground which can be cleared the better. But further work and further meetings may well be needed before an adequate total package can be achieved.

2. The Chancellor's paper is an amended version of the draft you saw earlier but is still disappointing. In particular it lacks clarity both in analysis and prescription, it dodges some important issues, and it is weak on the practical realities. For example:-

(a) The objective: This must be to end up next year with the lowest possible pay bill in the public sector consistent with avoiding disruption which would cost more than it would save and without creating unacceptable problems for the future. Although the Chancellor discusses a range of techniques to this end he nowhere assesses how effective they are likely to be, or balances risks against potential benefits. In your summing up of the May 19th meeting you asked for such an analysis but the Chancellor has not provided it.

(b) The central premise: The Chancellor's paper argues that what happens to public sector pay next year will have a direct influence on the outcome of pay bargaining in the private sector. This is a common assumption but is not easy to reconcile with the effects of monetary policy on the private sector. Of course the time lag inherent in comparability poses a problem and of course the Government needs to show that it is doing its bit over the whole field of its responsibilities. But there are dangers in basing policy on unproven assumptions particularly if the policy is to be pushed to the point of confrontation.

Rewrite these terms of reference.

(c) "Dethroning" comparability: The Chancellor's paper gives the impression that "dethroning" comparability, while maintaining it as one element in the system, is the key to success in reducing the real value of public service wages. But he does not explain what he means by "dethroning" in practical terms (just how would the Civil Service pay agreements need to be amended?). Nor does he explain how the creation of a wider margin for negotiation (the inevitable effect of "dethroning") would lead to a lower level of settlements. Certainly many in the public service unions think that they could do better outside the straitjacket of comparability by bargaining and confrontation (and it is significant that the Local Authority and Health Service unions show no signs of wanting to repeat last year's "Clegg" experiment). With due respect it is not enough to assume, as the Chancellor appears to do, that setting tough cash limits is the end of the matter. The prime casualty in confrontation could be the cash limit system. Once again, an informed guess at the likely magnitudes of the problems would be of considerable help to you and your colleagues. As Mr Biffen said at your meeting of 19 May, the cash limit itself is the key variable. To set it in a vacuum is to risk repeating the BSC experience on which John Hoskyns reported to you some weeks ago.

(d) Police and Firemen: The Chancellor says rather lamely that "these groups require more consideration than I have so far been able to give." But it is presumably unthinkable to set about reducing the real value of Forces' pay without also tackling Police and Firemen. Alternatively, if all three groups are excluded from the new arrangements, the arguments about comparability in the coming 12 months relate solely to

the Civil Service, the Doctors and Dentists and the TSRB groups, with the heart of the public sector pay problem - in the massed ranks of the employees of Local Authorities, the National Health Service and the Nationalised Industries - left to be dealt with, indirectly through RSG and EFLs. Early decisions on the Police and Firemen could clarify the dimensions of the problem.

(e) The future of "Clegg" etc: The Chancellor, surprisingly perhaps, comes down in favour of keeping something like the Clegg Commission in existence and possibly even amalgamating all of the present disparate pieces of pay machinery into a single whole. But he does not pursue his thought very far nor does he begin to explore the practical problems. It is perhaps worth making the point that the "Clegg Commission" as such has no separate supporting machinery (it relies on the Office of Manpower Economics and to a degree on PRU). It is not therefore impossible to envisage abolishing "Clegg" (which is in any case running out of work) while reviewing and revising the remaining machinery. At the same time it must be remembered that any attempt at creating a single body to take over the work of the PRU, the OME and the Review Bodies proper could run into formidable difficulties with their clients - eg the Doctors and Dentists. Perhaps the aim should be a common source of information and expertise rather than a single all-embracing institution. A good deal of work needs to be done before Ministers can sensibly come to decisions.

3. Of the other papers before the Committee, that from the Lord President (E(80) 48) is a powerful defence of the present Civil Service arrangements, coupled with a number of ideas as to how they might be improved. As far as the Civil Service is concerned, Ministers have a clear choice between the Lord President's approach and that sketched out by the Chancellor.

4. The CPRS paper (E(80) 49) introduces an interesting new idea in that it suggests that public service pay next year be tackled as a two-stage operation with interim settlements on the due dates and final settlements later when the downward trend in private sector pay will have become clearly established. As such it is an ingenious attempt to get over the "time-lag" problem in comparability. But it raises two problems: negotiability (which is essentially a matter of managerial judgement); and a shift from comparisons - formal or

otherwise - with the past to comparisons with the "going rate". If Ministers are attracted by this possibility it will need to be assessed in much greater depth before a judgement can be made.

5. The paper on public presentation (E(80) 47) is unlikely to cause much dispute between colleagues. Clearly there must be an educational process, and clearly a great deal of thought and effort will be needed if it is to make an impact. But these are matters for the professionals. The main input needed from colleagues is of their time for a centrally-mounted campaign presumably co-ordinated by the Paymaster General.

HANDLING

6. The main problem is likely to be to get your colleagues to focus coherently on the issues before them. It is perhaps inevitable that you should invite the Chancellor to speak first to his two papers, followed by the Lord President and Mr Ibbs. Thereafter, however, I suggest that you should try and focus discussion on those questions which there is a reasonable chance of settling now. For the rest it will be sufficient to commission further work.

7. Questions which it may be possible to settle at this meeting are:-

(a) The Civil Service: Do colleagues accept the approach of the Lord President in his paper or do they want to pursue the Chancellor's ideas of "dethroning" comparability? If the former, a clear decision is possible. If the latter, you will want to ask the Chancellor and the Lord President jointly to consider the practical implications of the Chancellor's ideas for the renegotiation of the Civil Service pay agreements. If however colleagues are unwilling to choose at this stage, more factual work will need to be done (see paragraph 9(a) below).

(b) Police and Firemen: Do colleagues agree that the pay arrangements for the Police and Fire Service should be re-examined with a view to breaking "index-linking"? If so, the Home Secretary and the Chancellor of the Exchequer should be invited jointly to produce a paper on what might be done.

(c) The Armed Forces: Do colleagues agree that the Terms of Reference of the Armed Forces Review Body should be revised to "dethrone"

comparability (bearing in mind that there is no scope for negotiation)? If so, the Secretary of State for Defence and the Chancellor of the Exchequer should be invited to produce proposals.

(d) The TSRB groups, including MPs: The Chancellor raises the question of whether the two reports from the TSRB expected later this month (one on the pay of senior Civil Servants, the senior Military, Judges and Nationalised Industry Board Members, the other on the pay of MPs) should be regarded as the final stage of the present round - and therefore accepted - or be used to set an example for the beginning of the next round. No decision need be taken until the reports are to hand. But colleagues will be conscious of the problems which the MPs report is likely to raise. If there is a disposition to make an example of the groups covered by these reports, the issues will have to go to Cabinet (both because of the Parliamentary implications and because Ministers with responsibility for particular groups - eg the Lord Chancellor for Judges - will want their say before final decisions are taken).

(e) The CPRS approach: If Ministers are attracted by the CPRS proposal it could be remitted to them for further study, in consultation with the relevant Departments, with a report back to the Committee in good time before the summer recess.

CONCLUSIONS

8. In so far as discussion allows, you will want to record specific conclusions on the points identified in the two preceding paragraphs. In addition it will probably be possible to record specific endorsement of the paper on publicity - E(80) 47 - and, depending on the progress made, to set a timetable for a further meeting or meetings of the Committee to bring matters to a conclusion, subject where necessary to endorsement by the Cabinet. The view the Committee takes on the approach to be adopted to the forthcoming TSRB reports will to some extent influence timing. If the implementation of these reports is to be regarded as a necessary, if unpleasant, consequence of past policies, your Committee has time to pursue its work in a fairly deliberate way. If on the other hand the inclination is to make an example of MPs and the other TSRB groups, there is a need for speed so that the decisions can be put in a broader context when they are announced - and the inevitable questions asked.

9. Other work which, subject to the discussion, might be put in hand includes:-

(a) Scenarios: The Chancellor should be urged to produce examples, as asked for at your meeting of 19 May, of the numerical relationship between pay, cash limits and the PSBR for each of the main public sector groups, together with an indication of the likely costs and results of industrial disputes in them. It is obviously far too soon to come to specific decisions about cash limits or EFLs for 1981/82 but an idea of the magnitudes involved would help colleagues to choose between the policy options open to them. This work will be particularly important if colleagues feel, as they may, that they do not know the sums of money at issue.

(b) Institutions: If the Chancellor's ideas of future institutional arrangements (including the continuation of "Clegg") are to be handled effectively, Ministers need a properly worked out set of proposals - including proposals for amending the Composition and Terms of Reference of the Review Bodies. The Chancellor could be invited to arrange for officials of the relevant Departments to produce a report. Unless colleagues feel disposed to abolish "Clegg" at once there would be advantage in waiting for such a report before coming to a final view on the Standing Commission. Abolition or continuation could then be set publicly in a coherent framework.

10. In addition it would be as well to record a specific conclusion inviting the Chancellor to bring his proposals for individual cash limits, including those for the RSG and for the pay content of EFLs, to the Committee in good time for their wider implications to be studied before final decisions are taken.

P Le CHEMINANT

Cabinet Office
4 June 1980