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PRIME MINISTER

NEW ARRANGEMENTS FOR DETERMINING THE SALARIES OF NATIONALISED INDUSTRY BOARD MEMBERS

1. On 7 July you announced that the Top Salaries Review Body would no longer be asked to advise on the salaries of nationalised industry board members. You said that in future these salaries would be determined by the Minister concerned in each case with the approval of the Minister for the Civil Service. In my minute of 1 July 1980 I proposed new arrangement for settling board members' pay from 1 April 1981. These were accepted by colleagues. Since then CSD officials have been consulting the Nationalised Industries Chairmen's Group. With the exception of the points below the Chairmen have agreed to the attached document which sets out the new arrangements (omitting of course the detailed procedures for consultation within the Government).
2. The Chairmen's Group's main concern is with the starting point of the new arrangements. We said that existing pay levels were inevitably the point of departure. Their attitude is that without any further review we should allow salaries up to the levels recommended in the last Review Body report (TSRB 14) to be implemented from each industry's settlement date during the year beginning 1 April 1981. They feel that if this is not accepted, it could prejudice the new system from the start.
3. The Chairmen's Group are in effect making two separate points. Under the new arrangements which we have proposed, major reviews of pay structure will normally require an independent report from management consultants. The Chairmen's first point is that for salary increases up to the levels recommended by TSRB 14 the TSRB Report ought to be sufficient evidence in itself without the need for costly and time consuming reports from outside consultants as well. I believe we can accept this in principle since outside consultants would consider the same sort of factors as TSRB and would be unlikely to make recommendations that were more soundly based.
4. However, the Chairmen are also saying that the Government should automatically accept increases up to the TSRB 14 levels during the coming year or possibly over a two-year transitional period. Indeed they have gone further and have suggested that these increases should be further enhanced in line with increases in senior staff salaries. We clearly cannot do any of these things. The Chairmen estimate that a "representative" board member requires a 9.6% increase to bring him up to the TSRB level (enhanced). In fact the average increase would be more like 11% and particular increases could go as high as 35%. I think the most we could say is that we recognise the problems, notably of differentials, to which TSRB 14 drew attention and that we will take these into account when considering individual proposals for increases.

CONFIDENTIAL

5. The Chairmen also asked us to consider again putting board salaries on a "board fee plus executive salary" basis. What this means is that full-time board members would get salaries as executives of their corporations, determined by the board itself as part of the salary structure of their management staff. On top of this they would get a relatively small board fee determined by the Government. I am against this procedure because it would mean that we would lose control of by far the largest part of board salaries. This would run counter to our decisions at E last May. The Chairmen have indicated to officials that they would be reluctantly prepared to accept the new arrangements without this aspect.

6. The final point which concerns the Chairmen is our inclusion of "the general economic climate" as a separate factor to be taken into account in considering pay increases. They want to change the last line of paragraph 5 of the document to read "... the performance of the industry within the context of the general economic climate". Here again I think that we ought to turn them down, for we must preserve our freedom to consider the national economic interest as a whole.

7. I therefore recommend that:

a) We should tell the Chairmen that we shall not need consultants' reports to justify increases in board salaries within the levels recommended by TSRB 14; but that although we will take into account the problems, notably of differentials, to which TSRB 14 drew attention we cannot commit ourselves to implementing increases to TSRB 14 levels during the next year or so.

b) We should confirm our rejection of the "board fee plus executive salary" idea.

c) We should insist that the general economic climate is a factor to be taken into account in its own right.

8. I would welcome your views and those of colleagues. I should like to receive them as soon as possible, since the new arrangements take effect from 1 April. When I have them I will arrange for a reply to be sent to the Chairmen's Group (I think that the Chairmen will want to pursue their case by making representations direct to Ministers, including perhaps yourself). We ought in due course to make a public announcement, perhaps by way of an arranged PQ, about the new arrangements. This would be much shorter and less detailed than the annexed note. I will let you have a draft when we have settled the outstanding points.

9. I am copying this letter to members of E, and to George Younger, Nicholas Edwards, Norman Fowler and Sir Robert Armstrong.

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PROPOSED NEW ARRANGEMENTS FOR DETERMINING THE
PAY OF PUBLIC BOARD MEMBERS

1. The Government has decided that the pay of members of nationalised industry and certain other public boards should be removed from the remit of the Top Salaries Review Body (TSRB) in order to give greater flexibility in settling pay levels. Ministers will retain their statutory responsibilities for these salaries and sponsor Ministers will play a larger part in determining them. However chairmen and non-executive directors will also have an important role. In addition there is a need for CSD to play a positive part. This memorandum proposes new arrangements for settling the pay of members of public boards of a commercial character in the light of these decisions.

2. A new system should so far as possible have the following features:

- i. It should be flexible enough to permit the nationalised industries to attract and retain satisfactory board members and to avoid problems of salary overlap with senior managers. It is to be expected that a more flexible system will lead to a wider range of pay levels both within the same board and between different boards.
- ii. There should be sufficient central co-ordination to ensure propriety, to maintain a broad balance between industries and to guard against leap-frogging.
- iii. The method of increasing pay should not give undue prominence to salary increases for board members.

3. Existing pay levels are inevitably the point of departure, although it is to be expected that they will be increased by the ordinary process of annual adjustment during the year beginning 1 April 1981. However from April 1981 new pay structures or pay levels for individual industries may be proposed if there is a clear need for them.

4. Proposals for new ranges or fixed points for full-time board members would generally in the first instance be made by the chairmen and non-executive board members and would need to be agreed by the sponsor Ministers after consultation with CSD Ministers. Recommendations on the chairman's salary could be formulated by the non-executive members without the participation of the chairman himself. The salaries of non-executive board members would be determined by the Minister in consultation with the chairman concerned but would normally not be less than the general level of the salaries of the full-time members of the same board scaled down by the proportion appropriate to the amount of time worked.

5. The essence of the move towards a more flexible system of pay determination is that pay increases would be based on managerial and market considerations and not on traditional comparisons and ranking between nationalised industries. The sort of factors which would be important would include the following: the need to recruit able enough people to the board, whether from inside or outside the industry; the need to retain and reward board members of experience and ability; internal differentials between board members and senior management staff; the performance of the industry; and the general economic climate.

Ordinary Periodic Adjustments

6. A distinction should be made between the procedures for ordinary periodic adjustments and for major reviews of pay structures, since the two involve different considerations. Ordinary periodic adjustments of board members' ranges or fixed points ought in general to lead to increases not greater in percentage terms than those granted to their own management staff. There could be presentational advantage in giving board members the same settlement date as their management staff so that separate announcements would not have to be made about their pay increases and not all boards would get an increase at the same time. Consideration would need to be given to the problem of transition from the present settlement date of 1 April. The positions of board members on their ranges would be reported to the sponsor department at the time of the annual pay review.

Major Reviews of Pay Structures

7. Where it was felt by the board itself, or by the sponsor department, that existing pay rates were seriously out of line with market requirements or that internal relativities were managerially unsatisfactory, a systematic case for a new pay level or structure would be made out. Unless the market or internal evidence was very strong, the recommendations of the chairman and non-executive directors would normally be supported by an independent report from management consultants with experience of pay determination for large commercial organisations. It would be open to the sponsor department to propose changes in pay when this appeared appropriate for any reason, for example, a change in the structure of the industry resulting in either more or less responsibility for the board. If any such change led to a proposal for a reduction in the general level of pay, the existing salaries of members already in post would be protected.