

PRIME MINISTER

cc. Mr. Hoskyns
Mr. Walters
Mr. Duguid

CPRS REPORT ON PAY

The CPRS were asked to report on the pay bargaining framework generally, and on pay determination machinery in the public services. These both remain central to the success or failure of the economic strategy, and therefore to the success or failure of the Government.

The main decisions required at your meeting on Monday concern the further work that should be done. We think the most fruitful areas for exploration are those listed below. They are not entirely drawn from the CPRS' recommendations: a note on each of those is attached at Flag A; and a separate note on why they should not pursue their principal suggestion, a "wage-inflation tax", is at Flag B. Until Megaw has reported, and we can start to set up market-based systems in the public sector, we are not attracted to radical alternatives to the present way in which pay is settled in the economy generally, and least of all to any of the various forms of incomes policies outlined in Section III of the Report. We think they are likely to be even more unsatisfactory than present arrangements, even if the coming pay round proves unexpectedly difficult.

A. THE GENERAL PAY BARGAINING FRAMEWORK

1. Getting a better result from arbitration

We agree that the Department of Employment should be asked to examine the prospects for getting affordability more clearly reflected in arbitration awards. It might be difficult to secure that, and it would certainly be difficult to ensure that the arbitrator did what he was supposed to do, but it may be possible at least to increase the weight which arbitrators attach to it.

/2. No strike agreements

2. No strike agreements in the context of new pay determination systems

A return to the pre-1971 no strike laws for public utilities would require effective sanctions. We think the exposure of trade union funds is an essential first step. No strike agreements might be an ingredient in public service agreements after the Megaw Report, especially if we move towards a more general framework of enforceable contracts.

3. Enabling employers to get labour cheaper

Enabling extra staff to be taken on at the lower end of the labour market means more jobs and helps to exert downward pressure on wages generally. If the abolition of Wages Councils is politically too hard to sell, then the CPRS proposal for removing their arbitral power to fix minimum pay would be the next best thing.

4. Cutting benefits to the unemployed

There are major political difficulties about lowering the real level of unemployment benefit or supplementary benefits. But their indexation against a background of falling levels of real pay reduces the incentive to work and inhibits the fall in wages. Professor Minford argues that a 10% cut in real benefits would reduce unemployment by half a million in two years. The Chancellor has raised this issue in the context of Merseyside. The political difficulties may increase as an election draws nearer.

5. Industrial relations legislation

We agree with CPRS that the benefits from changes in industrial relations law, important as they are, will emerge only slowly as the bargaining balance is affected.

/Mr. Tebbit

Mr. Tebbit will be making proposals separately, but it is useful that the CPRS now recognise:

- the importance of exposing union funds to produce an effective sanction against unlawful action, while reducing the risk of individual martyrdom;
- the importance of secret ballots.

The Policy Unit's paper on this also identifies these properties. But we think that it would be best to establish the new position for trade union funds before giving the Government a more direct role in disputes by taking power to order cooling-off periods.

On the right to lay off, CPRS do not distinguish two different EEF proposals: one is for a broad power to lay off anyone as a result of a strike in an essential service. This is too ambitious. But their more modest proposal is that a company or organisation should be able to lay off those white collar workers for whom there is no work as a result of strike action by fellow employees. This is a long overdue reform, necessary to head off the growing threat of selective strike action. The recent Civil Service strike provides a good example of the abuse of the present system.

B. IN THE PUBLIC SERVICES

6. What would be required if we wind up the Review Bodies?

The Review Bodies, generating comparability-based and often excessively high recommendations, cannot co-exist in their present form with cash limits. We think they

/should

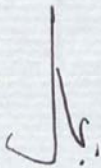
should all be wound up, or at the very least put on ice, unless they are prepared to accept a purely mechanical role. We ought to look at what the consequences would be, i.e. the subsidiary but quite difficult problems of dealing with the judiciary, doctors' expenses, armed forces relativities and so on.

7. The 1982/83 Pay Round

Ministers will naturally want to concentrate on improving the prospects for the pay round now starting. But we think it would be wrong to assume, as the CPRS does (Report, Paras 53 and 54) that by the time the 1982/83 round begins we shall have a market-based, post-Megaw system for the Civil Service - or that such a system may be applicable to other public services. It may well take a year to negotiate a post-Megaw agreement, and work ought to start soon on the role of cash limits in the next pay round, even though decisions will not be required until next summer.

Work on industrial relations legislation is, of course, proceeding separately; and social security benefits are primarily a public expenditure issue.

In our view, the other five issues should constitute the agenda for officials, and E(PSP), to work on with a view to reporting to Cabinet before Christmas.



J. M. VEREKER

18 September, 1981

POLICY UNIT VIEWS ON THE RECOMMENDATIONS

The CPRS list 12 recommendations:

(i) Watch the trend of settlements closely, so as to react if objectives are not being achieved.

We - through the Department of Employment - do this already. But we do not share the CPRS' pessimism about the likelihood of this pay round going seriously wrong.

(ii) More should be done to promote public understanding.

We believe that public understanding results from events and Government decisions, much more than from Ministerial speeches; but Ministers already make a major effort. Mr. Pym has already circulated a speaking note on the 4% pay factor, and has suggested it be used as a basis for discussions with employers - but most private sector employers don't need us to tell them of the virtues of pay restraint.

(iii) Management-employee communication should be encouraged.

MISC 14 has worked on this; Mr. Prior ran something of a campaign on it, with CBI and NEDC support. You gave it a boost with your speech at Bulmer's in Hereford. Of course this effort should continue.

(iv) Greater prominence for current cost accounting.

We agree: this might avoid employees getting a false impression of company profitability.

(v) Arbitration should be more responsive to affordability, unemployment and the national interest.

We agree, but there are real difficulties.

(vi) A step-by-step approach to industrial relations legislation.

Mr. Tebbit will make proposals. CPRS ideas reflect some of the right priorities: trade union funds and secret ballots. The ability

to lay-off white collar workers unable to work because of a strike by fellow employees is a priority. Cooling-off periods should only come later.

(vii) In the public services:

- (a) Pay factor not unrealistically low - already decided.
- (b) NHS pay factor should be 1% higher - to be considered in the public expenditure discussions; the decision should depend on the supply of and demand for NHS staff.
- (c) Arbitration and Review Bodies should be lectured on the consequences of excessive awards - they are already: and we think Review Bodies should be wound up.
- (d) Comparability for uniformed services should be ended - we agree.

(viii) In the public trading sector:

- (a) Present coal as a special case - we agree.
- (b) Face up to a strike on carefully chosen ground - we agree.
- (c) Emphasise the pay/productivity/performance/investment links - we agree.

(ix) Employment Subsidies

In general we do not favour employment subsidies: the present scheme, for young workers, was introduced as a "crisis measure" and we see no case for extending it.

(x) Cut in unemployment benefit

We agree that this would have a helpful effect on pay.

(xi) A statutory pay limit cannot be relied upon if drastic measures are required.

We agree; but we don't foresee a need for measures as drastic as that if the cash limit discipline is maintained. We would not rule out a freeze at the beginning of the round.

(xii) Further consideration of a Wage-Inflation Tax.

See Annex B.

THE PROPOSED "WAGE INFLATION TAX" (WIT)

The WIT is the report's main new recommendation for further work. It is described in detail on pages 42-44 of the report; its essence is that the Government would set a norm for pay increases, and impose a special tax on employers who paid more. We expect the CPRS to press strongly the case for further work to be done on such a scheme, as contingency planning against the day that a fundamental change in pay policy is needed to protect the economic strategy. We think the scheme has far too many inherent drawbacks to make it worthwhile looking at the details; and if it became known - which it would be - that we were considering such a scheme - there could be a rush for high settlements before it was introduced, thus making it inevitable.

The inherent weaknesses of the WIT are these:

1. It would have a perverse effect on incentives. Successful and profitable firms, who could pay their employees well, would be penalised. Market forces could no longer play a proper part in determining pay, which would to a large extent be established across the board by the Government.
2. It would operate more on the private sector than on the public. The concept of a norm for the private sector, which could not apply to the public services (Report, para. 118) and probably not to the nationalised industries, is the exact opposite of the Government's approach to pay. It would deny the logic that the Government's responsibility is for the pay of those it employs, and that pay elsewhere is largely determined by what other employers can afford.
3. It's not designed as an emergency measure, but as a permanent feature of pay bargaining arrangements. Layard, whose idea this is, conceived of it as an entirely new pay bargaining framework. In a crisis such as the CPRS postulate, the massive changes to our tax system could not be put in place quickly.

4. It wouldn't work.

It wouldn't work for two reasons. First, it would operate on the employer, not the employee, which is no good if the employees' bargaining power is strong (eventually the tax burden would simply bankrupt the employer). Second, there are too many ways round it: wage negotiations would keep the increase per hour within the norm, but overtime and fringe benefits would rocket.

5. It would be bureaucratic.

Not just new staff, but a whole new organisation, would be required to police the scheme, as well as the extra staff needed in related departments.