

DN
(arrived 1555)FROM: CHIEF SECRETARY
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PRIME MINISTER

3 OCTOBER CABINET: CONTROL OF RUNNING COSTS

I said that I would let you have a separate note on the handling of the discussion of running costs at Thursday's Cabinet.

2 The advantages of the move we have agreed to running costs targets ultimately in place of a manpower count are:

- (a) they make for better management. Departments can make cost-effective choices about how to discharge their responsibilities without decisions being distorted by marginal changes in civil service numbers;
- (b) they focus control where it is needed. Despite the fall in manpower numbers, civil service running costs have tended to increase over the last few years.

3 The transition to running costs is not straightforward. In particular, we cannot under running cost controls operate the old system whereby we set a pay assumption representing our negotiating target because running cost limits will not allow Departments automatically to raid their programme provision to meet higher pay settlements. They will have to look to other administration costs first. To achieve the managerial objectives at (a) above, we have to drop a central pay assumption and go for realistic departmental assessments (as explained in the Chancellor's note of 25 September).

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4 Some colleagues wish to re-open the question of running costs. They express concern about the presentational problem created by abandoning a central pay assumption, leaving Departments to defend their own provision for pay. Although they do not say it, I am sure that another factor is concern among Departments at the greater rigour which running cost controls will bring to bear on Departments' running costs. It will no longer be possible to switch spending on programmes to spending on administration.

5 In these circumstances, I propose to reiterate the advantages I see of a running cost control system as outlined above; and to suggest that the best way forward is to persuade those colleagues who have not yet settled to bring their provision for running costs down to more affordable levels.

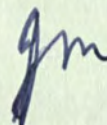
6 If concern persists, I will present colleagues with a choice. Either we keep to the policy of setting running cost limits; or we revert to the old system under which we base departmental cash limits on a 3 per cent pay assumption. This latter option is not an easy one. We have announced in public the move to running costs. Resurrecting the central pay assumption would mean re-opening agreements on running costs already reached (for which I would need authority in the Cabinet minutes); and it would be difficult to reconcile with the Government's intentions on a new pay regime for the civil service.

7 I think that faced with the choice, many colleagues would recognise the danger of losing the opportunity to establish a more management orientated system. But I would prefer to go back to the old system than attempt to find some halfway house of running cost limits based on, say,

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a 3 per cent assumption for pay. It has not in the past proved possible to absorb pay increases well in excess of 3 per cent within running costs alone. To suggest that it would be possible to do so in the future will raise even greater objections from colleagues than they are at present making to the system I am proposing. And in practice, there is a real danger that it would lead to wholesale breaches of running cost limits, discrediting a potentially useful system before it has time to get off the ground and become fully effective.



JOHN MacGREGOR

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