CONFIDENTIAL

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Chancellor of the Duchy of Lancaster

PRIME MINISTER

PERFORMANCE RELATED PAY AND UNIFIED GRADING

The Cabinet decided in July (CC(84)28 Conclusions) in favour of proceeding with a three year experimental scheme of performance bonuses for civil servants. This would begin in the financial year 1985-1986 and would apply to all staff in the grading levels from Grade 3 to Principal inclusive, at a cost of £4 million for each of the three years. The Cabinet agreed that officials should prepare detailed proposals to give effect to these conclusions for consideration by the Civil Service Ministers.

Officials have now prepared the attached proposed framework consisting of a set of draft rules and accompanying guidance. The framework envisages that permanent Heads of Departments should have a wide measure of discretion in designing and operating performance bonus arrangements. Discretion would extend to such matters as the size of individual bonus payments (subject to a minimum - designed to ensure that the money has a real impact and is not too thinly spread - of £500). Up to 1 in 5 of the staff at these levels would be able to earn a bonus for particularly good performance. Payments would be confidential to recipients. They would be made on the authority of the permanent Head of Department, and it would be made clear that Ministers would not be involved in individual bonus decisions. Sir Robert Armstrong has agreed that the guidance to accompany the rules should issue on his authority as Head of the Home Civil Service.

Permanent Secretaries have considered and accepted the draft framework. As the Cabinet recognised in July, the proposals are likely to be controversial amongst staff and there is also the danger of resentment amongst lower grades which are not included. Permanent Secretaries have stressed the need, therefore, for careful presentation of the proposals to staff and a readiness to consult the unions fully about their implementation. It is important that we announce the proposals without further delay so that there is adequate time for that consultative process before the experiments start on 1 April next.

I attach the draft of an announcement which, if you and the Chancellor of the Exchequer agree, I would like to make before the forthcoming Civil Service debate in the Lords, which means no later than 3 December. You will see that it lays stress on our willingness to consider the extension of the experiments to other grading levels. Appropriate steps would be taken to inform the staff and the unions when the announcement is made. I recognise that the answer is a little longer than is customary for a PQ reply but this seems to me to be justified in order to promote a better-informed debate in the Lords.

(Mr Hayhoe would answer a similar Question in the Commons.)

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It is also important in my view that we set the announcement in the wider context of our programme of Civil Service management reform. I am therefore anxious to include in the same announcement the proposed extension of unified grading to Principal level. On this members of the Cabinet have generally accepted my proposals, but the Secretary of State for Education and Science has reserved his position because of the implications for the science budget. Following further work by officials, I am writing separately to the Secretary of State inviting him to withdraw his objection.

Subject to resolving this issue, I would be grateful for your agreement that an announcement on the lines of the attached draft should be made on or before 3 December.

I am sending copies of this minute to the Chancellor of the Exchequer and to Sir Robert Armstrong and Sir Robin Ibbs.

GOWRIE
23 November 1984

ENCS

DRAFT

Q TO ASK HER MAJESTY'S GOVERNMENT: WHAT FURTHER STEPS ARE BEING TAKEN TO IMPROVE THE MANAGEMENT OF THE CIVIL SERVICE

A The programme of action I announced in July last year was directed at the improvement of the general quality of personnel management in the Civil Service as part of the Government's overall policy for improved management efficiency, and the achievement of better value for money by all civil servants. The introduction of performance related pay, and the further extension of unified grading were two important tasks under this programme.

On performance related pay the Government believe it right to provide additional incentives to good performance. This becomes more important in a contracting organisation, where there are reduced opportunities for promotion, which hitherto has been the main means of giving recognition to good performance. Performance related pay is widely recognised outside as a valuable management tool and has been recommended to the Civil Service on a number of occasions.

At the same time the successful introduction of this kind of arrangement into an organisation as large and complex as the Civil Service would be a major operation carrying with it significant changes in the functions of managers and their relationships with their staff. There are choices to be made about the form of a performance related pay scheme, as well as about its administration and the systems and procedures needed for that purpose. Cost is also an important factor.

For all these reasons, performance related pay cannot be introduced immediately across the whole of the Civil Service. But the Government consider it important that some steps should be taken. They therefore think it right to introduce with effect from 1 April 1985 an experimental scheme under which staff at the grading levels of Grade 3 (Under Secretary) down to Principal and equivalent grades will have the opportunity to earn a bonus for particularly good performance. The experiment will last for three years and its operation will be carefully monitored. A total of £4 million is being made available to fund this initial experimental scheme in each of the three years. This will not come from existing provision for Civil Service pay and related expenditure but it will be met from within planned public expenditure totals.

The Government will enter into immediate consultations with the Civil Service unions. It is also prepared to consider with the Civil Service unions the possible extension, within the three year period of the experiments, to other grading levels, subject to further consideration of method and finance.

The steps now announced will provide a basis on which the value and operation of performance related pay arrangements in the Civil Service can be tested, and enable decisions to be taken in the light of the experience gained as to any long term arrangements.

At the beginning of this year a major simplification of the pay and grading structure in the senior management levels of the Civil Service took place with the introduction of unified grading down to the Senior Principal level.

After careful examination, the Government has concluded that it would be right and worthwhile to extend unified grading to the Principal level. This would remove formal demarcations between occupational groups, and make it easier to get the right people into the jobs for which they are best fitted, at a level at which it is particularly important to broaden experience and develop senior management talent.

This further extension of the Open Structure to a new unified Grade 7 will enable a single pay structure to be created from some 100 currently separate grades, many with different salary scales, containing over 11,000 staff.

The unions will be fully consulted about the implementation of this change and a great deal of preparatory work will need to be done. The Government wishes, however, to implement this significant further reform on 1 April next year. The cost of aligning pay of the grades concerned, including any transitional arrangements which may be appropriate, will be met from within planned public expenditure provisions.

PERFORMANCE BONUS SCHEMES
DRAFT RULES

Introduction

As part of its policy to enhance the management performance and effectiveness of the Civil Service, the Government has decided to introduce an experimental programme of performance bonuses for individuals. It will be for each department to install and operate bonus arrangements. While the scheme is competitive, the aim must be to award bonuses in a way which can be seen to be reasonable and to apply standards which can be explained to staff. The departmental arrangements must conform to the Rules set out below, which may, however be subject to revision in the light of experience and evaluation during the experimental period. Additional notes for guidance are annexed for the assistance of departments, but these do not limit the discretion of the Head of Department as to the design and operation of bonus schemes beyond the Rules themselves. "Head of Department" in these rules means the permanent head of each department.

The rules applicable to any other grading levels to which experimental performance bonus schemes may be extended in the future will be issued as and when required.

Scope and Coverage

1. The initial schemes will operate for a three year experimental period commencing on 1 April 1985. All staff are to be within the scope of the initial scheme who are in the grading levels from Grade 3 to Principal level, including equivalent grading levels. Staff on loan between departments will be treated as members of the importing department. Exceptionally, a Head of Department may decide that particular groups of staff should stand outside the scheme.

2. The fund available for performance bonuses will approach 1% of the salary bill of the grades within the scope of the scheme as determined by Rule 1. But the distribution of the departmental fund as between the relevant grading levels, establishments and offices will be within the discretion of each Head of Department.

3. Performance bonuses will be taxable, and non-pensionable.

Criteria and Assessment

4. Those operating the schemes shall operate them so as to reward and encourage particularly good performance. Among the factors to be taken into account in judging whether a bonus should be awarded are:-

i) the extent to which the desired results have been achieved as a direct result of the individual's actions, taking account of the difficulty of their achievement;

ii) the energy and application shown in seeking to meet objectives and targets, including the exercise of qualities of leadership.

Distribution

5. The assessment of performance and decisions on the distribution of bonuses will be made by line management under the authority of the Head of Department.

6. Distribution of bonuses will be decided each year on the basis of performance over each separate assessment period as a whole. However, at the discretion of the Head of Department, not more than 10% of each department's bonus fund in any one year may be distributed as special bonuses to reward exceptional performance in particularly demanding tasks or situations at any time in the year.

7. The recipient of a bonus in one year is neither entitled to, nor disqualified from receipt of a bonus in any subsequent year. Not more than 20% of the staff within the scope of the scheme may receive a bonus in any one year. Special bonuses are outside this limitation.

8. The size of bonus payments may be determined under rules or guidance issued from time to time by the Head of Department. Payments may vary from one individual to another but no individual annual bonus payment shall be less than £500. Special bonuses may, however, be less than £500. Each payment will take the form of a single lump sum.

General

9. The names of recipients of bonuses will not be published, except that in the case of special bonuses publication is at departmental discretion.

10. The Head of Department will make arrangements to keep records, monitor and review the experimental schemes as a basis for assessing their effectiveness and operational efficiency.

PERFORMANCE BONUS SCHEMES

DRAFT NOTES FOR GUIDANCE BY THE HEAD OF THE HOME CIVIL SERVICE,
SIR ROBERT ARMSTRONG, GCB CVO

Introduction

1. The Rules of the experimental performance bonus schemes are intended to provide the basic framework within which all departmental schemes will operate in the Civil Service. They provide a foundation of consistency to which all schemes will conform, but are also intended to permit departments the opportunity to reflect in their individual schemes different requirements which their differing roles, organisation and management structure demand. They are also intended to provide us with information about the results of different approaches to the operation of performance bonuses to help us assess the advice to be given to Ministers at the end of the experimental period.

2. Nevertheless, I believe that departments may welcome some further notes for guidance on how their schemes may be designed and operated, and that is the purpose of this paper. But while these guidelines supplement the Rules, they do not limit the discretion of the Head of Department beyond the Rules themselves.

Scope and Coverage

3. (Rule 1) We start from the position that all staff at the relevant grading levels are to be within the scope of the scheme. It is acknowledged that special considerations may affect the way in which the performance of particular individuals or groups is assessed, for example, staff who move posts during the assessment period, staff on long training courses, recent promotees, the staff of Minister's offices, groups whose conditions already include some kind of performance pay, etc. It will be for the Head of Department to decide what supplementary arrangements may be needed in the application of the schemes to such staff, or whether indeed in exceptional cases they should be excluded altogether from their operation. Ad hoc arrangements will need to be made between the departments concerned to cover the position of staff moving on loan from one department to another during the year.

Criteria and Assessment

4. (Rule 4) Performance bonuses are intended to contribute to improving the overall effectiveness of the organisation, by encouraging and rewarding

particularly good performance and, in addition, seeking to enhance motivation more generally. The criteria are intended to reflect these broad aims and to take account of the diminishing availability of promotion as an incentive to good performance. However, I must emphasise that there is an essentially competitive element in the assessments to be made. The approach requires the distribution of a limited bonus fund between staff in the eligible grades according to judgements as to the relative performance of individuals.

5. (Rule 4) It is important for both effectiveness and presentation that assessments should be based so far as possible on known factors directed primarily towards the attainment of the objectives of the organisation, taking account of the difficulties of their achievement. One important element in the present drive to improve financial management in government departments is the setting of clearer objectives for the department as a whole and for its staff, accompanied by the improved development of measures which can be used to assess progress and performance in achieving those objectives. It must be acknowledged, however, that, especially among the more senior levels covered by this experimental scheme, a large subjective element will necessarily be present in performance assessments.

6. (Rule 4) Assessments may be made in such form as departments decide. For reasons set out in paragraphs 4 and 5 above, and because of other reasons of practicability, I can see that we cannot specify immediately a link of general and automatic application between assessment for bonus awards and the current staff reporting and appraisal procedures. But since both are based upon the same performance by the individual concerned, broad consistency between them is certainly to be expected.

Distribution

7. (Rule 5) The Head of Department will decide on the allocation of responsibility for decisions on the award of bonuses. We would expect that decisions on specific awards would normally be taken at least two levels in the line management hierarchy above that of the individual concerned. Subject to maintaining the cardinal responsibility of line management for judging performance, Heads of Department will wish to make arrangements aimed at achieving a reasonable degree of consistency in the assessment standards applied and the smooth working of the scheme. Departments may wish, for example, to establish moderating mechanisms, which, however should not detract from the

responsibility of each line management concerned for individual assessments.

Ministers have agreed that they will not be involved in individual decisions on performance bonus awards

8. (Rules 7 and 8) In determining the size and number of bonuses to be awarded from the funds available, Heads of Departments will need to take account of the overall aims of the experiments. The specific limitations within which departments may exercise this discretion are the 20% ceiling on the proportion of eligible staff who may receive awards and the minimum annual bonus payment of £500. In applying these we need to ensure that bonuses are sufficiently exceptional in number and amount as to act as a real incentive to individuals and a discipline on management judgements, but not so exceptional as to be seen by the majority as virtually unattainable, while also bearing in mind the controversy which might result from very large payments in individual cases.

General

9. (Rule 6) The timing of bonus assessments is for departments to decide provided that payments are made within the financial year to which the funds relate. Unspent funds cannot be carried over.

10. There is no requirement to set up any special appeals procedure, but staff will have access to normal existing grievance procedures. I am confident that in administering the scheme departments will guard against the possibility of claims of unfavourable treatment on grounds of race or sex.

11. Finally, I intend that decisions as to the form any longer term arrangements will be taken in the light of experience with the experimental schemes. Progress will be monitored and assessed under arrangements to be approved by me in due course, but departments will be directly accountable for their expenditure on bonuses and will need to monitor the working of the schemes. I envisage that we will need to set up liaison arrangements to ensure that our monitoring arrangements avoid duplication and are compatible.

R T ARMSTRONG

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