

SUBJECT.



FILE
bcc: Mr. Vereker
MJ

cc: Noster set.

10 DOWNING STREET

From the Private Secretary

16 June 1982

Dear Peter,

Index-Linked Pensions

The Prime Minister held a meeting this morning to discuss the matters raised in the Chancellor's undated minute received here on 15 June. Apart from the Chancellor, the Home Secretary, the Lord President, the Secretary of State for Social Services and the Secretary of State for Employment were also present.

The Chancellor said that in the Cabinet discussion on 3 June colleagues were moving towards a decision to retain index-linking, to place the full burden of its cost on beneficiaries on a pay-as-you-go basis, and to raise the extra contributions by means of a special levy rather than by altering the details of each public service pension scheme. This policy was consistent with the stance which Ministers had taken in the pre-election period in 1979; and it accorded well with the findings of the public opinion poll recently carried out for the Conservative Party. There was much pressure in the House to announce the Government's decision before the House rose for the summer recess. It had to be recognised, however, that there were problems about the timing of an announcement, and about dropping a piece of major legislation in the 1982/83 programme to make room for a pensions bill. There was also concern about the effect of an announcement, whenever it came, on the current pay round. His conclusion was that the Government should make an early announcement, whether before or after the recess, on the lines of that attached to his minute, to the effect that there would be consultation, a White Paper at the turn of the year, and legislation at the beginning of the next Parliament.

In discussion it was suggested that it was a matter for regret that there appeared to be no alternative to dealing with this problem other than by removing index-linking altogether or by dealing with contributions. There were, however, powerful reasons for reaching an early conclusion on this matter. There was much genuine resentment on the part of those who were not beneficiaries of index-linked pensions but were obliged to pay for the index-linking enjoyed by others. It was unjust that there should be two nations,

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one enjoying this considerable benefit and the other not, but both contributing towards it. The poll to which the Chancellor had referred, however, illustrated the extent to which index-linking had become established as part of the expectation of a wide group. Given the difficulty of removing a benefit already enjoyed by so many, the Chancellor's conclusion that action should be taken on contributions seemed inescapable. The only practical way forward was the scheme proposed by the Chancellor, which was one of a rough justice. It would be important to extend the principles of such a scheme to the nationalised industries, whose employees should not in equity fare better than those in the public services in this regard.

Against this, it was argued that an announcement on the lines proposed by the Chancellor would have a serious effect on the wage round. There could be no question of making the announcement during the National Health Service dispute, since it would add another bone of contention to an already difficult position. Indeed, whenever the announcement was made, it would have awkward implications both for pay, and for inflation prospects generally. Arguably, it was a higher priority for the Government to maintain its progress on inflation than to risk this by taking the desired action on pensions; and further progress on reducing inflation would also serve to make less acute the resentment about index-linking. What was proposed might achieve the worst of all worlds; the announcement would cause acute difficulty on the pay front, but by postponing its implementation until the next Parliament, and by preserving index-linking, there would be little immediate political benefit. Finally, it was doubtful whether the scheme could be extended with success to the nationalised industries: there would be great problems about ensuring that increased pension contributions were not financed by higher pay.

Summing up the discussion, the Prime Minister said that the Lord President should arrange for a debate in the Parliamentary overspill, in October. This should be a low-key occasion, at which the Government sought to expose the complexities of the issue, without committing itself firmly to any particular conclusion. In the debate the Government could reveal its hand a little more clearly than on previous occasions, in particular on the principle that it was a matter of simple justice that those groups who enjoyed index-linking should, broadly, pay for the benefit; it would be desirable to give close attention to the attitude of the Opposition parties to this principle.

I am sending copies of this letter to the Private Secretaries to the Home Secretary, the Lord President, the Secretaries of State for Social Services and Employment; and to David Wright (Cabinet Office).

Yours sincerely,

Michael Scholar

Peter Jenkins Esq
HM Treasury.

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