

Week End Box

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Ridley's Memo

COVERING SECRET

TO ALL MEMBERS OF THE LEADER'S CONSULTATIVE COMMITTEE

The Research Department have been asked to prepare the two enclosed papers - Operation of Incremental Scales under Pay Restraint (LCC/76/112) and The Monetary Approach to Forecasting Inflation (LCC/76/113) - and to circulate them for this evening's discussion by the Shadow Cabinet on incomes policy under Item 4 of the Agenda.

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AMR/MEM  
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OPERATION OF INCREMENTAL SCALES UNDER PAY RESTRAINT

[Paper by the Research Department]

Sir Geoffrey Howe has suggested that the problems of incremental scales are significant enough to warrant the Shadow Cabinet's reaching an agreed view on them. This note sets out the chief issues involved.

I INTRODUCTION

The continuation of payments under incremental scales during periods of pay restraint is a constant source of controversy. Criticism arises on two grounds.

- a. It seems to mean that some people get more than the limit to which everyone is supposed to be held. This causes particular ill-feeling because non-industrial Civil Servants are amongst those covered by incremental scales. The suspicion therefore arises that they always formulate the rules to their own advantage.
- b. The granting of pay increases to individuals above the limit would appear, prima facie, to imply exceeding the overall increase in the pay bill consistent with the limit.

The issue has arisen once more because it is clear that such payments are to be permitted under the 5% limit, as they were during the £6 year.

II DO SOME GET MORE THAN OTHERS?

The principle behind incremental scales is that salaries should increase by clearly defined amounts in accordance with age, length of service, merit or improved performance. It usually applies only to salaried staff and to apprentices moving up to the full rate for the job. Progression up incremental scales tends to be more or less automatic. This does mean that those who are on such scales can expect to obtain more than the limit set for pay increases. Two points, however, should be noted:

1. other wage earners, mainly manual workers, can receive pay increases above the limit for 'improved performance' under payment by results schemes and through working more overtime and shiftwork,
2. employees of almost any kind, particularly salaried staff not covered by fixed incremental scales, can be rewarded by 'promotion' which will raise their pay by more than the limit.

III IS THE RESULT INFLATIONARY?

In theory, incremental scales should balance and their operation should not be inflationary. Recruitments and transfers at the bottom should be balanced by promotions and retirements at the top. In other words, as a man moves to the third year position on a salary band, another should be leaving through promotion to a different grade and a further person should be coming in at the first year position. The assumption behind this is that the age profile of the workforce and the numbers employed remain constant. Where such stability does not exist it can, in principle at least, be allowed for.

In practice, the operation of the scales can be either inflationary or disinflationary.

They can be inflationary if a company chooses to bend the pay policy rules and recruit under-qualified staff at the second or third 'rung' in a salary scale rather than at the first 'rung'. They can be disinflationary if management replaces third 'rung' employees with

others paid at second 'rung' rates or lower. The direction in which they operate is probably dictated by the state of the labour market.

#### IV SHOULD THE PAYMENT BE DISCONTINUED?

There is clearly some understandable discontent about the continuance of these payments. They do arbitrarily discriminate against those who either have less formal arrangements or who were in the process of reviewing a formal arrangement when the new pay controls were introduced. But the extent to which this favours those on incremental scales can be exaggerated.

- a. Employers who do not have such schemes can still find other ways of rewarding employees over the limit. Further, employees who feel they are falling behind because they have no incremental scales can seek other jobs at higher rates elsewhere; many of those on incremental scales work in the public sector where alternative employment opportunities are fewer.
- b. Freezing of incremental scales would produce anomalous results in the reverse direction; those who had fixed scales and promotional procedures would be unable to reward merit etc., whilst those who did not could continue to pay increases through spurious promotions.
- c. The incremental scales are, in any case, part of agreed pay structures, and the payments will have to be made eventually (e.g. a man cannot be employed forever on a 17 year old apprentice rate). If they are not made now, they will lead to a sharp increase in labour costs later, particularly in the public sector, when controls are lifted. So to suspend their operation will add further to the sense of injustice felt by these many groups hard done by during pay restraint, without generating any long-run advantage.

If the Conservatives were now to advocate discontinuing incremental payments, it would be inconsistent with the stance adopted by the Party in Government, and might well be seen as opportunism.

If civil servants and the public sector are using incremental scales to reward themselves disproportionately, that fact should emerge eventually from the researches of the pay research unit (suspended at present) and more quickly from the Department of Employment's new earnings indices. Remedial action which would probably involve restructuring their schemes could be proposed accordingly at that stage. At present, there is no evidence to suggest that it is happening.

If it were felt that the situation needed further investigation in order to establish what is happening beyond all reasonable doubt, then there are a number of channels which could be used.

#### V CONCLUSIONS AND RECOMMENDATION

We conclude that:

- (a) there is not a strong case for suspending the operation of incremental scales during periods of pay restraint;
- (b) to do so would not restrain wage pressure permanently but would defer it to the future;
- (c) there are no grounds for believing that increments as such are being abused.

We therefore recommend that their operation should not be opposed.

It is for further consideration whether more information should be gathered to test conclusion (c) immediately above.