

*✓ Mr Verdon
Mr Duggan
Am not very happy about the
synopsis - not
fundamental*



Prime Minister

*Cabinet office will be
sending a brief, for the
meeting on Wednesday*

PRIME MINISTER

*enough in the 20, 25, 30
Revising in the 20, 25, 30
Discretionary on points
for water in minutes
Proposed in minutes
Point - pay needs
not*

*St Peter's Club
10.7.*

I welcome the suggestion in your Private Secretary's letter of 2 July of an early meeting to consider the handling of Government evidence to the Civil Service pay inquiry under Sir John Megaw, and I attach to this minute a synopsis of a suggested approach.

The inquiry will require a good deal of factual background material; the preparation of this is in hand. But more important will be how we present our views on the shortcomings of the present pay system and on the points we want the inquiry to consider in particular. We need to reach early agreement on this framework.

In his minute to you of 7 July the Chancellor of the Exchequer suggests that we should first consider the inter-departmental report by officials prepared some time ago on Civil Service pay arrangements. As he says many of the issues raised by the report are relevant to our evidence and we can draw on it in presenting the arguments to the Committee. Indeed we could set about framing a set of detailed proposals for a new system to put to the Committee. But I think that would be the wrong approach for us to take, for I would not want the inquiry to see itself or to appear as sitting in judgment on a Government scheme. For that would seriously reduce our room for manoeuvre after we have its report.

We shall need to cover a number of topics:-

a. Nature of new pay system

We need new arrangements better able to meet the requirements of varying economic circumstances. We have also said that we want an "ordered and agreed" system, i.e. one to which both Government and unions are hopefully prepared to be committed to minimise the risk of recurring industrial trouble. We must not suggest that we are not prepared to look on its merits at a "committed" system providing it offers sufficient safeguards.

b. Role of cost and economic circumstances

As the report by officials clearly brings out there are very difficult questions to be faced in securing arrangements which though ordered ones enable the Government to meet its wider economic responsibilities in controlling public expenditure. The report discusses various options for dealing with this dilemma. I do not think that we need to choose between them now for the purposes of our evidence to the Committee. What we must do is to make it clear that questions of cost and economic circumstances have to be taken into account as a sine qua non. We should show ourselves ready to examine any recommendations by the

Committee for reconciling these wider requirements with a reasonably stable system of pay determination.

c. Arbitration

We do not want to offer any firm guarantees now about the future of arbitration. But if we were to suggest in our evidence that arbitration will not normally be available in future this would have a serious effect on our industrial relations and our attempts to rebuild these. We do not need to precipitate a conflict now on arbitration as an issue of principle. We can underline the need for the Government to be able to withhold arbitration on policy grounds but say that a view will have to be taken on the role of arbitration in the light of the new pay system which emerges from the Committee's work and the Government's subsequent discussion with the unions.

d. Pay factors

We regard it as essential that "market" factors such as recruitment, retention and relative job security be included in this new system.

e. Pay comparisons

We have said that comparisons should continue to have a part to play. If the comparisons are to be valid ones they must be based primarily on outside rates. But the report by officials suggests ways in which the present pay research arrangements are defective and which must be remedied in making comparisons under a new system.

Other aspects

f. I want the Committee to consider some specific issues on the framework of Civil Service pay rates. These include the role of internal relativities; the scope for greater geographical differentiation in Civil Service pay rates; the future of incremental scales; the case for merit pay and the scope for productivity bargaining.

No doubt as its work proceeds the Committee will want more detailed evidence on particular issues. We can also expect to be asked to comment on the evidence submitted by others including the unions (who will no doubt be asked to comment on ours). But I propose that the Government's initial evidence to the Committee should be on the lines which I have suggested. As background for our discussion it might be helpful for colleagues to have the attached synopsis of the ground that it would cover.

I am copying this minute to the Home Secretary, Chancellor of the Exchequer, the Secretaries of State for Employment, Defence and Social Services, the Chancellor of the Duchy of Lancaster, the Attorney General and Sir Robert Armstrong.

S.

CONFIDENTIAL

SYNOPSIS OF GOVERNMENT EVIDENCE TO THE INQUIRY ON CIVIL SERVICE PAY

INTRODUCTORY

1. Present arrangements no longer command confidence. Priestley Commission reported 25 years ago at a time of full employment and low inflation. Very different position now. Need for system capable of responding to changes in economic circumstances. Need to take account of recent problems thrown up by Pay Agreements.

APPROACH TO A NEW PAY SYSTEM

2. Government's aim is "ordered and agreed system" to which both sides can be committed. Desirable as basis for avoiding industrial disputes involving central Government directly. Scope for "no strikes" agreement?

3. Advantage if Committee can recommend procedures to keep increases in Civil Service pay more in line with those in pay generally. Present system leads to "out of phase" settlements causing real and presentational problems.

4. Full range of "market factors" important in fixing pay. Comparison with outside rates on its own inadequate. "Market factors" of recruitment and retention position (assessed against forward manpower requirements) should play more direct part than under Priestley approach. Also relative job security. Committee invited to make recommendations on practical methods of assessing these factors for pay purposes.

5. Cost and economic circumstances also need to be taken into account. Future arrangements must enable Government to meet its general economic responsibilities in controlling public expenditure. Government will occasionally need to curtail Civil Service pay increases in national interest even if justified on management grounds. Possible options include "override" for use in exceptional circumstances or more direct application year-by-year of cost and economic factors. But Government ready to examine ways of reconciling wider economic requirements with a stable system of pay determination. This objective is essential.

6. Government committed to finding means of reconciling procedures for fixing cash limits and negotiating Civil Service pay. Various options including possible change in operative date of Civil Service pay settlements.

Future arbitration arrangements best considered in light of decisions on pay system following Committee's report.

PAY COMPARISONS

8. Comparisons have an evident part to play, for Civil Service pay levels cannot be held below outside rates for any lengthy period of time without serious management problems. Comparisons need to be based primarily on outside rates for similar work.

9. Functional comparisons can readily be made where outside jobs have close similarity to Civil Service work, eg clerical jobs. More difficult at senior management levels. Committee asked to examine reliability of comparisons at different grading levels. Institutional arrangements required for fact-finding to be considered in light of PRUB's observations on scope for wider role for any successor body. Committee asked to consider relationship of new system to TSRB's work on pay of senior grades.

10. Specific points:-

- a. Comparisons to be based on much more representative sample of outside employers. Committee to examine suggestion of excluding public sector; and ways to extend comparisons with private sector including wider and more representative spread of firms.
- b. Outside pay rates need adjusting for differences in other benefits and conditions. Stringent assessment needed of value of "fringe benefits".
- c. To what extent is it necessary to consider "up-to-date" aspects of pay comparisons? "Uprating" procedures linked to price movements one of the most unsatisfactory aspects of the old system.

OTHER ASPECTS OF NEW SYSTEM

11. Committee invited to consider:-

- a. role for internal relativities;
- b. use of incremental scales;
- c. case for merit pay and scope for productivity bargaining at more junior levels;
- d. scope for greater geographical differentiation as alternative to present system of national rates plus London Weighting.

CONCLUSION

12. Committee asked to advise on both principles to form basis of new pay system and practical arrangements for applying. Terms of reference leave it free to examine any aspect of Civil Service management practice relevant to this.