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12 December 1980

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CABINET
MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY
PAY REVIEW BODIES

Note by the Chancellor of the Exchequer

I attach a note prepared by Treasury officials in consultation with the other Departments concerned. I agree with their analysis and recommend the following approach to my colleagues:-

- (i) We should accept the helpful offer in the letter of 21 November from the TSRB to advise on the distribution of a limited amount of money, and ask the TSRB and DDRB to give advice within constraints reflecting our approach to cash limits for 1981-82.
- (ii) We should try to persuade the two Review Bodies to confine themselves to such advice; but we must recognize that this may not prove possible.
- (iii) If they are not willing to confine themselves in this way, we are likely to face embarrassing recommendations in due course; the only way of avoiding that would be through formally amending their terms of reference or suspending their operation. Either of these courses would have disadvantages, as the official report brings out. But they are possibilities we must discuss.

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(iv) The question of the AFPRB requires special consideration because of our public commitments. But my view is that serious damage would be done to our policy for pay in the public services if we implemented recommendations of the AFPRB which meant giving the forces much bigger pay increases than others in the service of the central government. I think we could reasonably argue that, at least in the circumstances of the current pay round, the "civilian counterparts" of the Armed Forces are primarily in the other public services and that broadly the same financial discipline should apply. This would point to handling the AFPRB in the same way as the TSRB and DDRB this year.

(v) Whatever our decision on the AFPRB, our evidence to all these Review Bodies should draw attention to the need to take account of current economic conditions and of the financial constraints that apply to the public services.

G.H.

HM TREASURY
12 December 1980

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PAY REVIEW BODIES

Note by Treasury Officials

This note considers possible action in the current pay round towards the three pay Review Bodies. It is not concerned with possible longer-term changes, which are being considered as part of the current study of future arrangements for pay determination in the public services.

2. This note has been prepared after consultation with officials in the Civil Service Department, Ministry of Defence, Department of Employment, DHSS, No 10, CPRS and Cabinet Office; but other departments are not committed to the arguments or the recommendations in it.

Background

3. There are three bodies involved: the Armed Forces Pay Review Body (AFPRB), the Top Salaries Review Body (TSRB), and the Doctors and Dentists Review Body (DDRB). Details of each of these bodies are set out in Annex A. All have a purely advisory role. It is for the Government, in the light of their advice, to take decisions on the pay of the groups concerned. However, successive Governments have indicated that they would not reject or modify recommendations from the Review Bodies unless there were obviously compelling reasons for doing so.

4. Ministers last considered their attitude to the Review Bodies in July. The discussion took place in the context of the longer-term future of pay determination, including the future of the Clegg Commission. As a result, it was announced that the Clegg Commission would be wound up, but that the Review Bodies would continue to operate.

5. Ministers have made a number of public statements regarding the operation of the Review Bodies. These are listed in Annex B. In summary, however:

- (a) Ministers have undertaken that the AFPRB will continue to operate on a basis of comparability with civilian counterparts.
- (b) The Prime Minister has stated that all three Review Bodies should continue to make recommendations.

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(c) The Government has asked the TSRB to review the third stage increase in the pay of MPs.

The Problem

6. The Government has announced that the rate support grant and grants to universities will be calculated on the assumption of an increase in 6% in earnings from annual settlement dates; and that the pay of other public services will be subject to broadly the same financial disciplines. However, the AFPRB will undoubtedly, as matters now stand, base its recommendations on comparisons with movements in earnings in the economy at large; and the DDRB has given considerable weight to that factor in the past. Comparisons with movements in earnings would point to increases of the order of 15-20%. The TSRB could also be expected to take account of such comparisons; and in their case there is the further factor that their recommendations in 1980 were reduced by the Government by an average of 12%.

7. There is therefore a high risk that the Review Bodies will come forward with recommendations for pay increases which are embarrassing in themselves, which could cause problems in persuading other groups to settle for increases of around 6%, and which, at least in some cases, would be difficult to accommodate within cash limits. Paragraphs 11-17 below consider whether anything should be done to reduce or remove this risk.

Special position of AFPRB

8. First however, it is necessary to consider the special position of the AFPRB.
(a) On the one hand, Ministers have entered into public commitments to the effect that the AFPRB will continue to operate on the basis of comparability. This will be widely regarded as implying continued operation on the basis of comparison with earnings movements in the rest of the economy. Ministers have also agreed that the relevant cash limit will be increased, if necessary, to cover pay increases following the recommendations of the AFPRB.

* The figure of 6% has been adopted only for the RSG and grants to universities; for the other public services it is at this stage only a planning assumption. In this note it is used as shorthand for "6% or whatever other figure Ministers may approve for determining cash limits".

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(b) On the other hand, to give the Armed Forces special treatment in this way would make it considerably more difficult to constrain pay increases within the 6% allowance, both in the public services generally and in the particular case of the other two Review Bodies. It could be argued that, at least in the circumstances of the current pay round, "civilian counterparts" of the Armed Forces should be regarded as primarily the other public services.

9. This issue can only be decided by Ministers; and the rest of this note accordingly concentrates on the TSRB and DDRB.

10. But, whatever Ministers may decide about the APPRB, Government evidence to it can draw attention to general economic factors and the need for restraint in pay awards, and can point out that there are factors related to pay (such as allowances and quartering charges) and pensions (on which the forthcoming Scott Report may be helpful) which would justify a lower pay settlement.

Possible change in terms of reference

11. As noted in Annex A, the terms of reference of the Review Bodies are very wide. They neither require nor prohibit taking account of general economic circumstances and the ability of the country to pay; and the Government is free to present evidence on both these aspects. The TSRB, however, in a letter of 21 November to the Prime Minister (Annex C) has made it clear that it considers that its duty is to recommend what it judges to be the "right" levels of pay. Any reduction is a matter for the Government. The attitude of the DDRB is harder to predict. In the past, it has been receptive to Government evidence on the economic situation and the need for pay restraint. But this has usually been in the context of an announced pay policy applying to the whole economy. A more diffuse restraint relating to public expenditure rather than pay as such and applying only to parts of the public services is a different matter.

12. There is therefore a case for amending the terms of reference of the TSRB and DDRB to require them to take account of general economic and financial considerations. However -

(a) the Review Bodies already do take account of such considerations. There is a risk that they might come up with much the same recommendations as under their existing terms of reference; but it would then be more difficult to reject them.

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(b) To meet this point, it would be possible to draft the terms of reference so tightly as to give the Review Bodies little option but to recommend increases of the order of 6%. But it is unlikely that they would agree to operate under such terms, since they would in effect be asked to take responsibility for a decision by Government.

(c) A change in the terms of reference could prove a false move in the context of the longer-term studies referred to in paragraph 1 above; it could also make it more difficult to develop a coherent policy for all three Review Bodies. If Ministers decided to treat the AFPRB as a special case during the current pay round (see paragraphs 8 and 9 above).

Suspension

13. Another possibility would be to suspend the TSRB and DDRB for the current pay round, for much the same reasons as pay research was suspended for the non-industrial Civil Service.

(a) It will be much easier to persuade other groups to accept 6% if there are no embarrassingly inconsistent recommendations regarding "correct" levels of pay. Such recommendations can serve no purpose except to provide the Government's critics with ammunition.

(b) The Government's policy is to pay only what the nation can afford. What the Review Bodies may recommend regarding "correct" pay levels is irrelevant in current circumstances.

(c) Suspension might have a useful effect on public opinion as illustrating the need to avoid excessive pay increases.

14. There are, however, also good arguments against suspension.

(d) The Government's policy relates to expenditure, not pay increases as such: it does not feature a 6% pay norm. To suspend the TSRB and DDRB would imply that the Government intended directly to determine pay rates (without advice), rather than to impose a constraint on public expenditure. If the Government decided to suspend the DDRB it would face very serious technical problems for the assessment of general medical and dental practitioners' pay.

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(e) Although the degree of commitment is much less than in the case of the AFPRB, suspension could still be represented as inconsistent with the Prime Minister's statement in July.

(f) Total suspension of the TSRB would, in fact, be very difficult since the Government has asked it to report on MPs pay. But once the Government begins picking and choosing, the difficulties increase and the advantages lessen.

(g) Suspension of the DDRB would create an immediate and long drawn out row with the professions. If, as is possible, the DDRB recommendations are in line with the Government's expenditure assumptions, such a row is unnecessary; and if the current pay round goes well, the professions will have less reason to complain if pay increases consistent with the 6% assumption are imposed on them.

15. Finally, it is relevant that the Review Bodies report relatively late in the pay round. The DDRB normally reports in April, with its report published in May; the TSRB usually follows a similar timetable, though it was late in 1980. Thus the reports are unlikely to have a significant effect on expectations during the current round: by the time they are published, the tone will long since have been set.

A limited remit

16. A less drastic course of action would be to ask the Review Bodies to advise the Government on the distribution of pay increases, subject to a constraint that the cost of the increase for each group concerned should not exceed 6%. The TSRB has already offered to do this, in its letter of 21 November; and there is no reason to suppose that the DDRB would refuse, though this would need to be confirmed with them. This approach would conform to Government policy, but would allow the Review Bodies to discharge the useful, in some cases almost essential, role of advising on distribution.

17. It would be highly desirable, from the Government's stand point, if the Review Bodies confined their recommendations to such an exercise, and said nothing further about "correct" levels of pay. It is possible that the DDRB may be prepared to do this, although the letter of 21 November suggests

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that the TSRB will probably not. It would, however, be possible to sound the two bodies out informally.

Summary

18. The essential problem is that the Government has announced that the rate support grant and grants to universities will be calculated on the assumption of an increase of 6% in earnings from annual settlement dates, and that the pay of other public services will be subject to broadly the same financial disciplines; but that there is a high risk that the Review Bodies will come forward with recommendations that will create difficulties for this policy. The following considerations are relevant to possible action to deal with this problem.

(a) The Government's public commitments towards the Armed Forces could be interpreted as requiring that the AFPRB should continue to operate on the basis of comparisons with earnings movements in the rest of the economy. However, this will create serious difficulties for the Government's policy on pay restraint; and other interpretations of the commitments are possible. This is a matter for Ministers to decide; and the AFPRB is therefore largely excluded from the main discussion in the note. Whatever the decision, Government evidence to the AFPRB can stress the need for pay restraint and point out factors justifying a lower pay settlement.

(b) There is a case for amending the terms of reference of the TSRB and DDRB to require them to take account of general economic and financial considerations. This would reduce the risk of the Review Bodies producing embarrassing recommendations. But it would not remove the risk; it might increase the difficulty of rejecting embarrassing recommendations; and it could prove a false move in the longer term.

(c) Another course would be to suspend the TSRB and DDRB, for reasons similar to those which led Ministers to suspend pay research for the non-industrial Civil Service. However, this would be more appropriate to a pay, rather than an expenditure, policy; and it would create serious problems with the medical professions.

(d) Finally, it would be possible to ask the TSRB and DDRB to advise on the distribution of pay increases, subject to a constraint that the cost of the increase for each group should not exceed 6%. The TSRB has already indicated its willingness to offer such advice.

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(e) It would be best, from the Government's standpoint, if the
TSRB and DDRB confined their recommendations to such an exercise.
The two bodies could be sounded out informally on this point.

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THE PAY REVIEW BODIES

The three Review Bodies all have similar terms of reference: to advise the Prime Minister on the remuneration of the group concerned. In other respects, however they diverge.

Method of working

AFPRB: Has well-established (and fairly sophisticated) machinery for factorial comparisons. Much of the input is in the form of job evaluation reports by consultants; and the outcome thereafter is essentially mechanical.

DDRB: since there are no obvious outside analogues for Doctors and Dentists, and the DDRB has steered clear of factorial comparisons, the recommendations rely largely on applying judgement to earnings movements in the economy at large as evidenced by the New Earnings Survey.

TSRB: uses surveys of top management salaries, plus a considerable element of judgement. The TSRB has stated that it adjusts its recommendations downwards to take account of differences between the circumstances of the public and private sectors.

Treatment of pay within public expenditure system

AFPRB: the pay of the Armed Forces is cash limited; but for 1981-82 it has been agreed that the cash limit will be adjusted if necessary to accommodate the pay settlement.

DDRB: salaried doctors and dentists (just over half the total) are covered by the NHS cash limit. The pay of family practitioners is not cash limited.

TSRB: all groups, except most judges, Ministers and MPs are cash limited; but the small numbers of people involved, in relation to the total pay bill, means that the cash limits in practice need not constrain the size of the settlement.

GOVERNMENT STATEMENTS REGARDING THE WORK OF THE PAY REVIEW BODIES

AFPRB

- (a) The Election Manifesto promised to "give Servicemen decent living conditions, bring their pay up to full comparability with their civilian counterparts immediately and keep it there".
- (b) Mr Pym announced in a press statement on 10 May 1979 that "having fulfilled its undertaking by restoring the pay of servicemen to the level of their counterparts, it is the Government's intention to maintain it thereafter at those levels".
- (c) The Prime Minister said on 10 July 1980 that she would honour the recommendations of the AFPRB in respect of the Armed Forces (Hansard column 756).
- (d) In answer to Parliamentary Question on 2 December, Mr Pym said that "the Government will continue to fulfill its commitment to maintain Forces pay at the levels of their civilian counterparts. The actual increase to be awarded next year will depend upon the recommendations of the Review Body on Armed Forces Pay".

Other Review Bodies

On 4 August 1980, the Prime Minister said that the Government had decided that the three pay Review Bodies should continue to make recommendations on the groups within their terms of reference (Hansard column 50).

TSRB

On 21 July 1980, the Leader of the House announced that the Government had agreed "that the Review Body should be asked to review next year's third stage increase of hon Members pay to £13,150" (Hansard column 165); a formal letter on these lines was sent to the TSRB on 8 August.

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Annex C

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The Rt Hon Margaret Thatcher MP
10 Downing Street
London SW 1

Dear Prime Minister

21 November 1980

My colleagues on the Top Salaries Review Body have told me about your discussion with them following the lunch on 7 November 1980, which I am very sorry not to have been able to attend; and it may be helpful if together with Edwin Plowden who is taking the chair when I am absent, I attempt to clarify our understanding of the Review Body's position in the light of the points you have raised; particularly as to the bearing on our work of economic priorities as defined by the Government.

Our role as we see it is essentially to indicate what we consider to be appropriate levels of remuneration for the groups within our remit, having regard to such factors as the need to attract and retain individuals of suitable calibre, relevant pay comparisons, though I should add that we are not and never have been committed to any simple doctrine of comparability for these groups, and differentials within a given pay structure. In exercising this role it is crucial that we act, and are seen to act, as an independent body; it is not for us, as I am sure you would agree, to attempt to act as arbiters on matters which lie within the economic or political domain.

The Government of course in putting evidence to us may wish to draw attention to economic considerations which it regards as important, and if it so desires may inform the Review Body that it would not find it feasible to implement total increases beyond a certain limit. In that event we should naturally refer to such evidence in our report, but we would not regard it as part of our function to comment on its merits or to take it into account by recommending levels of remuneration lower than we judged to be 'right'.

Once we have reported, the Government will have to decide what shall be done; and we recognise that the Government might take the view that the exceptional economic circumstances justified it in modifying or setting aside our findings. Such an outcome would not in itself be inconsistent either with our independence or with our ability in the long run to continue to do a useful job; our independence would on the other hand be gravely undermined were we to become involved in questions of general policy, or of what can finally be afforded, which must rest with the Government itself.

I think it only right to say, however, that in view of the Government's decision to reduce substantially the amounts we judged to be appropriate under our criteria as from 1 April 1980, it seems inevitable that the results of our present review, although it will be some time before we are able to quantify them, will point to increases of a significant order in the salaries which were actually implemented.

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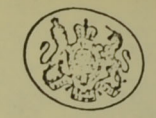
151

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- 2 -

Nonetheless, if the Government decided after receiving our report that it could not allow such increases to be implemented because of overriding economic circumstances, but wished to seek our advice on how the limited amount available could best be distributed to maintain sensible salary structures, we would be ready to provide assistance in that respect.

We are very grateful to you for saying that you will issue a further public statement about the Review Body's position. It was of course only last July that you gave an answer to a written Parliamentary Question, which we welcomed, making it clear that the Government wished the Review Body to continue; but given the way events have moved on since then, a fresh statement in some form is clearly desirable to avoid the growth of speculation; as you will have seen, some rather misleading comments have already appeared in the press. Insofar as the statement might seek to define the Review Body's position in the changed conditions which now exist, we would much appreciate an opportunity to comment on it in draft.

Yours sincerely

Boyle of Handsworth

BOYLE OF HANDSWORTH, CHAIRMAN
REVIEW BODY ON TOP SALARIES

Plowden

PLOWDEN

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