

**CONFIDENTIAL**

THIS DOCUMENT IS THE PROPERTY OF HER BRITANNIC MAJESTY'S GOVERNMENT  
E(80) 8

8 February 1980

COPY NO 55

CABINET  
MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

—————  
PUBLIC SERVICE PAY NEGOTIATING MACHINERY  
Note by the Chancellor of the Exchequer  
—————

The paper by officials poses a very real dilemma. Instinctively, I am sure, most of our feelings incline towards encouraging decentralised bargaining, and the paper identifies the advantages that could result from this. On the other hand, there are undoubtedly severe risks in any change which stem from the simple fact that trade union negotiators will seek to turn any situation to their advantage. Officials have quite rightly identified effective financial limits and financial control as key elements if there is to be any successful move to decentralised bargaining. But equally, they point out that past experience in this kind of direction suggests that in general unions have achieved their objectives at management's expense. If we are to achieve our objectives in the future, substantial changes from this past pattern will be essential. This means more effective financial control, stronger management, and stronger links between finance and the pay bargainers.

The paper points out, in the Annex, that the areas where this can be achieved, at least in the short term, are limited. Further, it suggests that the scope for limited experimentation is very small, and regards the risks of major change in large pay groups as very considerable. Accordingly officials suggest a study of the one public service area (local authorities) where

**CONFIDENTIAL**

CONFIDENTIAL

there is any significant degree of decentralised bargaining, coupled with moves towards greater geographical pay differentiation and management responsibility (whether or not achieved through full decentralised bargaining) in other suitable areas.

I invite colleagues to consider the paper.

G H

HM TREASURY

8 February 1980

CONFIDENTIAL

**CONFIDENTIAL**

PUBLIC SERVICE PAY NEGOTIATING MACHINERY

Note by officials

1. Cabinet (CC(79)14th meeting, item 6) invited the Chancellor of the Exchequer, in consultation with the Lord President of the Council and other Ministers as appropriate, to arrange for officials to consider the desirability of changes in the existing systems for settling the pay of suitable public sector groups, in the light of the Government's evolving policies for cash limits. We have taken this, in the light of the Cabinet discussion, as requiring us to consider possible decentralisation of pay bargaining in the public services.

Background

2. With a few minor exceptions, all the non-trading public services are widely dispersed geographically; nevertheless pay negotiations are mostly centralised. This pattern is by no means confined to the public services. The same picture holds in many nationalised industries, and in much of the private sector - both across industries (eg banks) and in large companies (eg some car manufacturers, ICI). Such centralisation makes possible central cost control over all aspects of pay, and can help to eliminate (or at least constrain) leap-frogging between pay of groups at different locations, and the proliferation of locally-negotiated bonuses, 'incentive' schemes and other payments, which may reflect as much the pressures on line managers to get the job done as what can be afforded, or what is justified by the output of the workforce. On the other hand, central negotiation involving national rates for particular groups cannot reflect differences in the state of the labour market throughout the country, and if set to secure a barely adequate labour supply in the most difficult areas, will certainly be higher than required elsewhere. Thus many firms with effective financial control over decentralised units (GEC is a notable example) have preferred decentralised bargaining. Further, in some situations at least, firms have decided to move to local negotiations on productivity payments in an attempt to ensure that payments are justified by the productivity actually achieved

**CONFIDENTIAL**

**CONFIDENTIAL**

(BSC are an obvious example).

3. It is not self-evident which is the preferable approach. Nor is there necessarily a universal preference: the circumstances of different groups vary widely. In the private sector there have been moves both to and away from centralised bargaining, as companies attempt to secure greater cost control and managerial accountability. It follows that each pay group must be considered individually and the balance of advantage for or against change weighed. Further, the choice is not a simple one between centralisation or de-centralisation: there is a variety of intermediate choices.

General objectives of decentralised bargaining

4. The basic objective, against which any proposal for decentralisation must be judged, is to improve the efficiency of the labour market, and to make it more responsive to local circumstances, thus helping to reduce unit costs. This would aim to reflect those factors - supply and demand, regional differences, efficiency - which Ministers have identified as relevant to public sector pay determination and which could be influenced by a change of bargaining patterns. (It must not be forgotten, however, that the internal labour market - the relationships between the terms and conditions of those already employed in an organisation - can be just as important where efficiency is concerned.) The objective might be achieved through:

- a) geographical variations of rates, which might arise automatically under decentralised bargaining, but could also be sought by agreed central negotiation of eg regional variations. London Weighting and big city allowances in the private sector already provide examples of this. They are however additions to national pay rates: and they are based on differences in the cost of living, not in the demand and supply of labour.
- b) Responsiveness to local markets: an extension of the geographical variation principle to take account of finer local variations and market pressures, which could only be achieved in local negotiation. This will not however be possible where, as for many pay groups, the market is a national rather than a local one: the scope for geographical pay differentiation would then

**CONFIDENTIAL**

**CONFIDENTIAL**

be limited to the possibility of making allowance for the greater or lesser attractiveness of certain localities (including their lower or higher cost of living).

- c) Deepening management responsibility: direct local responsibility for pay and conditions could deepen and strengthen the whole process of local staff management: it could lead to a more positive and effective approach to identifying and eradicating, by negotiation or otherwise, inefficient practices, which generally needs to be done at local level.
- d) the opportunities which may exist for exercising more direct financial control by bringing together responsibility for pay and finance.

These possibilities should be seen as means to an end, not objectives in their own right: though (c) and (d) both carry with them wider and desirable advantages.

Risks

5. Trade unions would be likely to resist decentralisation because it would reduce the role of national union officials (which may be an advantage from the Government's point of view), operate against their concept of a 'fair rate for the job' and reduce the potential power of the unions to secure it. Accordingly any change may involve a price - either financial or, if decentralisation is pushed through by management, in terms of more difficult negotiations and loss of employee co-operation.

6. It must be expected that unions would seek to exploit any change towards decentralisation to increase wages beyond what they would otherwise have been:

**CONFIDENTIAL**

CONFIDENTIAL

CONFIDENTIAL

a) They might try to maintain national minimum rates and negotiate local variations over and above these (an arrangement already formalised, for example, in the engineering industry). Indeed, they will no doubt try to make the national rate the same as it would have been if there had been no change to decentralised bargaining. Whether or not these tactics would succeed depends upon the toughness of management, the effectiveness of the financial constraints on management, and the power balance between management and unions. But it must be said that past experience points strongly towards the unions achieving their objectives at the expense of management.

b) Leap-frogging would be an obvious risk. Again much the same arguments apply as in (a) above. Organisations where there is a single employer, and where there is a long-standing uniformity of pay treatment which the unions are expert at enforcing (eg the Civil Service) will be particularly at risk. In recent years there have been a number of moves to introduce centralised bargaining precisely to break an established and very expensive leap-frogging pattern between different local bargaining units - British Leyland and British Shipbuilders are notable examples of this. Unless local managements are both strong and effectively financially constrained, the unions will simply pick them off and then generalise their gains. Local productivity deals should be at less risk of this than local negotiations on basic rates, or on terms and conditions: but even here, powerful forces operate to encourage 'evening up'.

c) A move to decentralisation would put negotiations into the hands of people currently less experienced in pay bargaining: this might work either way, but the risk would be that unions would gain in many cases, and use those gains for subsequent dragging up of other groups. It cannot be assumed that line managers, faced with a job which has to be done to a certain

CONFIDENTIAL

CONFIDENTIAL

CONFIDENTIAL

CONFIDENTIAL

schedule and a pay claim backed by threats of industrial action which would make that schedule impossible to achieve, will not seek to buy out trouble, even if it means putting their finances at risk.

- d) Cash limits may not in themselves be a sufficient financial constraint. Within a cash limit, and without centralised control over pay, there would be nothing to stop local management from 'end-loading' a settlement (ie spreading the settlement through the year so that there was a higher increase at the end than at the beginning) which would automatically increase the base line for the following year's cash limit. This could be another fruitful source of leap-frogging.

Financial control and management freedom

7. In our view, necessary conditions for fully decentralised pay bargaining (though not for geographical differentiation) are that clear financial limits, the ability to exercise financial control, and the ability to take effective management decisions, exist at the level of the decentralised bargaining unit. If such conditions do not exist, there will not be the constraint on and support for the management pay negotiators to enable them to resist union pressures and to trade off the level of pay settlements against staff numbers, productivity or level of service provided.

8. The annex to this paper considers briefly the main public service groups, and concludes that the main areas where such conditions at present exist are local authorities, the national health service and some groups within the industrial civil service. Even for these groups, it will be difficult, if not impossible, to adapt the financial control mechanism to take full advantage of decentralised bargaining: for to do so, financial limits should be set for each bargaining unit so as to reflect local labour market factors and other variations. Obviously, the more the bargaining units, the more complex and difficult the task: the risk would be that in setting local cash limits, there would inevitably be some errors which would lead to quite illogical pressures being placed on local managers.

CONFIDENTIAL

CONFIDENTIAL

CONFIDENTIAL

CONFIDENTIAL

Further, the present RSG arrangements - with grant being paid as a constant proportion of marginal expenditure - militates against such an adjustment; the proposals for a new block grant system will provide for some variation of the rate of grant on marginal expenditure at the top of the scale but that will not affect the majority of authorities in this respect.

9. If Ministers wish to proceed further with the idea of decentralised pay bargaining, we recommend concentrating on groups which already have suitable financial control arrangements and adequate management freedom. They provide a ready-made test-bed: if decentralised bargaining will not work there, it is still less likely to work elsewhere given the much deeper changes that would be required. This however is not to say that other changes to improve the responsiveness of pay bargaining to geographical differences, but short of full decentralised bargaining, should not be tested in the meantime.

Proposals

10. We suggest the following ways forward:

- a) Local Authorities. By choice the annual negotiations on pay and on most conditions of service for directly employed staff are carried out centrally, but the individual authorities negotiate 'occasional items', in particular incentive bonus and productivity schemes and the local application of some nationally agreed conditions and grading standards. This pattern of negotiation and the fact that the locally negotiated elements produce wide variations in earnings among the authorities suggest that a study to examine the following might be of value:
  - i) how much local autonomy is there in practice
  - ii) how effective is it and what are the problems (NB Clegg's comments on efficiency payments, which are all locally negotiated)

CONFIDENTIAL

CONFIDENTIAL



**CONFIDENTIAL**

- iii) how effective is the financial control over the local negotiations
- iv) how have management and unions adapted to this pattern of bargaining
- v) how the authorities see the relative advantages and disadvantages of central bargaining
- vi) whether the existence of separate Scottish bargaining arrangements has led to significantly different rates. But Government has no statutory locus in local authority establishment matters and therefore no basis on which to force local authorities to change their existing practices. Nor at present are there established grounds on which to encourage them to move towards decentralised bargaining. Even a limited study on the lines proposed above would raise the suspicions of LACSAB (the central negotiating body) and the Associations about its motives, and, however careful the handling and presentation, it might not be possible to secure the co-operation from them which would be needed if the study were to be effective.

b) National Health Service. Although the financial and management structure makes this a possible test-bed candidate, the fact that there is shortly to be a major reorganisation in our view rules it out at present. Trying to alter the pay bargaining arrangements at the same time, or indeed until the reorganisation has settled down, would simply be too disruptive: though it would be worth having the possibility of decentralised bargaining in mind during the reorganisation to ensure that nothing inimical to decentralised bargaining is created during the reorganisation. However, this need not inhibit other moves to bring financial and management responsibility and pay bargaining in the NHS closer together. The Management Sides of the Whitley Councils are made up of representatives of NHS management in Great Britain and the Health Departments, the former being in a majority. Because the cost of pay agreements is wholly met from the Exchequer and implementation

**CONFIDENTIAL**

**CONFIDENTIAL**

requires Ministerial approval the convention has been established that Management Sides seek approval before making offers. Hitherto such approval has related to the cost and principal terms of each offer. In the coming negotiations it is hoped that the Health Departments will be able to disengage from detailed approval and that Management Sides collectively will settle individual offers within the overall cash limit. However this involves a major new task which they are viewing with caution and reserve and it may be necessary in this round for the Health Departments to retain responsibility for keeping offers within the cash limit. Meanwhile Management Sides are considering how best to introduce more flexibility into the Whitley Agreements, which would enable local management to have more discretion, mainly in the grading of posts.

- c) Non-industrial civil service. As indicated in the Annex, the structure of the civil service creates very grave difficulties in the way of any system of local pay bargaining. A number of the lower grades are however non-mobile, and form part of local labour markets: setting a national pay rate for these grades can mean that they are over-paid in some areas and under-paid in others. Accordingly the CSD are considering in detail whether there is scope for geographical pay variations amongst the non-mobile grades, by taking account of regional pay variations in national negotiations.
  
- d) Industrial civil service. As indicated in the Annex, while basic pay for the industrial civil service is determined nationally, productivity and incentive schemes are locally negotiated. For many groups, the same financial and management problems arise as for non-industrials, though geographical pay rates negotiated nationally are again a possibility. But there are some areas within the industrial civil service which form effective financial and management units, and where decentralised pay bargaining might be introduced. Obvious possibilities

**CONFIDENTIAL**

CONFIDENTIAL

are where trading funds exist. One such case is the Royal Ordnance Factories. CSD and MoD Ministers have already agreed to examine, for MoD industrials as a whole, the possibility of a degree of decentralisation in relation to productivity bargaining and allowances. We doubt if Ministers will wish to launch a further exercise until this is completed. Another case is the Stationery Office, which is to become a trading fund on 1 April. Here we suggest a study which would look at the present bargaining arrangements and possible options for making them more decentralised: in the light of this Ministers could consider which, if any, of the options they wished to adopt.

Summary and Conclusions

11. The basic objective, against which any proposal for decentralisation must be judged is to improve the efficiency of the labour market, and to make it more responsive to local circumstances, thus helping to reduce unit costs. This objective might be achieved through geographical variations of rates, responsiveness to local markets, strengthening management responsibility and exercising more direct financial control. (para 4).

12. There are risks. Trade Unions would be likely to resist decentralisation because it would reduce the role of national union officials, operate against the concept of a "fair rate for the job" and reduce the potential power of the unions to secure it. They would seek to exploit any change towards decentralisation to increase wages beyond what they would otherwise have been by negotiating local variations over and above national minimum rates and there would be a risk of leap-frogging. A move to decentralisation would put negotiations into less experienced hands and cash limits may not in themselves be a sufficient financial constraint. (paras 5 - 6).

13. The necessary conditions for fully decentralised pay bargaining (though not for geographical differentiation) are the existence of clear financial limits, the ability to exercise financial control and the ability to take effective management decisions. The main areas where such conditions at present exist are local authorities, the national health

CONFIDENTIAL

CONFIDENTIAL

CONFIDENTIAL

services and some groups within the industrial civil service. Ministers are recommended to concentrate on these groups if they wish to proceed further with the idea of decentralised pay bargaining. (paras 7 - 9).

14. The following ways forward are suggested:

- a) a study of decentralised pay bargaining in local authorities;
- b) the pending reorganisation of the National Health Service rules out decentralised bargaining at present but this need not inhibit other moves to bring financial and management responsibility and pay bargaining in the NHS closer together;
- c) the structure of the non-industrial civil service creates grave difficulties in the way of local pay bargaining and accordingly the CSD are considering in detail whether there is scope for geographical pay variations amongst the non-mobile grades;
- d) there are some areas within the industrial civil service where decentralised pay bargaining might be introduced eg where trading funds exist. The possibility of some degree of decentralisation in MoD in relation to productivity bargaining and allowances is already being examined and a study might be made of possible options for more decentralisation in the Stationery Office. (para 10).

CONFIDENTIAL

CONFIDENTIAL

CONFIDENTIAL

ANNEX

FINANCIAL CONTROL AND MANAGEMENT FREEDOM

1. The major area where suitable conditions already exist is local authorities. Their constitutional position and financial structure gives them the scope to exercise these conditions so far as their own staffs are concerned, and indeed their position is strengthened by their powers to raise finance through the rates and to charge for certain services. However it should be noted that, although individual local authorities are in no way bound to negotiate pay centrally, they have deliberately chosen to do so on many aspects of pay. Further, their constitutional position means that the Government cannot force them to change their negotiating arrangements - though it could, of course, seek to exercise persuasion.
  
2. The position with regard to other groups of local authority employees is rather different. Primary and secondary teachers, for example, are in England and Wales, and by local and island authorities in Scotland, employed by the 104 local education authorities. Financing, as for other local authority services, is through RSG and rates, but the Remuneration of Teachers Acts provide for national negotiations leading to pay rates with statutory force. Areas of local discretion in grading are built into the statutory system and London weighting is paid. These arrangements are regarded as appropriate for a national service employing a very mobile qualified labour force.
  
3. To take another local authority field, the police are statutorily maintained by police authorities which, except in the case of the Metropolitan Police District, are closely related to local authorities. 50% of police expenditure is directly met by the Government, 50% by precept on local authorities (though this element is eligible for RSG). National rates of pay are prescribed by the Secretary of State, but central government control over current expenditure is essentially limited only by the Secretary of State's determination of numbers on the police establishment: although this control may be adequate when pay is negotiated nationally, it would not be an adequate constraint on decentralised pay negotiations. Any change in the existing arrangements would require legislation.

CONFIDENTIAL

CONFIDENTIAL

4. The financial structure and control arrangements for the National Health Service would certainly permit decentralised bargaining, since funds are effectively allocated to the main employing level (Area Health Authorities in England and Wales, and Health Boards in Scotland). Unlike local authorities, however, it has no independent source of funds, and the fact it is, and is intended to provide, a national service places constraints on the ability of local management to vary levels of service.

5. The same argument about the need to provide a national service applies, generally speaking, to the non-industrial civil service. But even greater difficulties are caused by the fact that, outside London, much of the civil service is organised, not in large blocks that form suitable negotiating units, but in small local offices (employment, social security, revenue) or a cluster of regional offices of different departments. If bargaining were by local offices, it would not be practicable to set cash limits down to this level of detail: further, where different offices were drawing on the same local labour market, the inevitable result would be leap-frogging. If on the other hand, offices were grouped into larger bargaining units on cross-departmental lines, this would make nonsense of the lines of financial and management responsibility, as well as requiring a radical reconstruction of the whole of the present financial structure and method of accounting to Parliament, which is at present set entirely in Departmental terms.

6. The position of the industrial civil service is more diverse. While basic pay and conditions are determined nationally, productivity and incentive schemes are locally negotiated. In terms of financial arrangements, for many the picture described in the previous paragraph applies. Others form distinct financial and management units albeit on a national basis, eg the Royal Ordnance Factories (which have operated under a trading fund since 1974) and the Stationery Office (which is to move on to a trading fund in April this year). But there are limitations on how far this can be applied. For example earlier studies of the possibility of a trading fund for the dockyards came to nothing because, as near-monopoly suppliers of services to the Royal Navy, they do not operate in a truly commercial trading environment. An attempt between 1967-70 to have a specific system of wage rates for the

CONFIDENTIAL

CONFIDENTIAL

CONFIDENTIAL

dockyards and for three other functions broke down because the employees (and indeed line managers) were continually comparing wage rates in different establishments and refused to accept that differences in industrial function justified significant differences in pay for the same work.

CONFIDENTIAL

CONFIDENTIAL