

Prime Minister

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PRIME MINISTER

cc Mr Mount

E: Megaw

We have consistently advised you against the adoption of a Megaw type pay determination system for the Civil Service, because we do not believe the Megaw proposals adequately satisfy our criteria of affordability and market factors. The further work by officials on safeguards has certainly produced proposals which will limit the drawbacks of a Megaw system, but they do not remove our fundamental objections. We believe that the introduction of Megaw into the Civil Service, which is bound to be followed and imitated elsewhere in the public services, will rigidify pay bargaining and hinder our efforts to reach a state in which no pay increases are automatic, and all are related to profitability, productivity and performance.

Nonetheless we do not suggest you hold out against the Chancellor's recommendation that we open negotiations with the unions on the basis of Megaw, for two reasons:

(i) Most if not all of your colleagues would be content with a Megaw type system, and indeed those responsible for other public services (such as the NHS and the Police) are already contemplating the introduction of similar arrangements;

(ii) Since Megaw is widely (but in our view, wrongly) regarded as offering what the Government wanted, we would be accused of setting up the inquiry in bad faith if we now announced that we do not like the recommendations. There would certainly be a vigorous reaction from the Civil Service unions, who begin their special pay conferences next week.

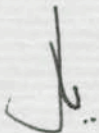
I suggest therefore that there is no point in resisting the recommendation of the Chancellor's Group (MISC 83) to the effect

that Megaw should be accepted as a basis for seeking to negotiate a new pay system. The important decision for E is over safeguards, the subject of the supplementary report by the Official Group.

In my view, the safeguards recommended by the Official Group meet your concerns, notably about the danger of a new system committing the Government to finance a pay increase it cannot afford. Apart from the right to terminate any new Pay Agreement at six months notice, officials recommend that the Government should have the right to impose a settlement outside the interquartile range, subject to the approval of the House of Commons, which could be sought if the Government judged national economic circumstances required it. The unions will certainly resist this, because it gives the Government the power to override the outcome of the process of comparisons; but it is no more than any employer has a right to insist upon.

The officials' supplementary report comes down against getting recruitment, retention and job security data into the comparison process, but concludes that the possibility of this could be looked at early in the life of the new system. It is unlikely that your colleagues will be prepared to accept the fundamental change that would be implied by diluting comparability with market factors in this way, but we would much prefer it.

The Chancellor will no doubt warn his colleagues that the negotiators will have difficulty in reaching a new Pay Agreement on the basis of Megaw plus safeguards. And indeed the unions' pay conferences may instruct their executives not to negotiate. But if negotiations do take place, the two points of difficulty for the unions are points on which I am quite sure we should make no concession: access to arbitration only by agreement, and imposition. It would be helpful if that is made clear to the negotiators from the outset.

  
1 December 1982



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The Megaw Report

I agree generally with Mr. Peter Gregson's brief for E Committee's discussion of the Megaw Report tomorrow.

2. Though clearly the Government should not be prepared to embark upon negotiations with the unions on the Megaw Report unless it is genuinely prepared to reach agreement on that basis, Ministers are not now being asked to commit themselves to every detail in Megaw as a basis for agreement. They have been asked simply to accept the Megaw recommendations as a basis for negotiations on a new pay system.

3. MISC 83 concluded that the Government should accept the recommendations as a basis for negotiations. If, subject to satisfactory resolution of the points you yourself have raised, E Committee endorses that conclusion, that will in my view have advantages for the Government, both in its relations with its own staff and in its dealings with the unions.

4. It was the Government that terminated the old pay agreement; and that decision upset a great many members of the staff and provided militants in the unions with a cause which they could exploit. It was then the Government which set up Megaw. If the Government can now show that it is prepared to negotiate on a new pay system, based on Megaw, that is likely to help relations with staff throughout the Civil Service, not least in handling the pay settlements for April 1983.

5. There could be no certainty that the unions would be able to agree among themselves to negotiate on the basis of Megaw, let alone to reach agreement. The two largest unions, the Society of Civil and Public Servants and the Civil and Public Services Association, whose Executives are now heavily dominated by the left, are holding special conferences this month, and may try to prevent negotiations. If there is to be failure to



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negotiate, it will be preferable that the onus for that failure should be placed upon the unions rather than upon the Government. It would help to avoid further weakening of the moderates in the unions if the Government were to show that for its part it was prepared to negotiate on the basis of Megaw; and in that event the blame for failure would rest with the unions and would put them at a disadvantage.

RA

Robert Armstrong

1st December 1982



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The Megaw Report

BACKGROUND

The Report of the Inquiry into Civil Service Pay under Sir John Megaw was published in July. It proposed a new system of pay determination in the Civil Service, of which the main features would be as follows:

✓ a. The governing principle should be to ensure that civil servants were paid enough to recruit, retain and motivate them to perform efficiently the duties required of them at an appropriate level of competence.

b. Annual pay increases should be confined to the range between the lower and upper quartile of movements in the pay of comparable workers in the private sector: the point within this interquartile range would be a matter for negotiation in the light of market factors and affordability.

X c. Every four years there should be a review of total remuneration levels both within the Civil Service and of comparable workers outside; if the review showed that there had been unacceptable changes in Civil Service pay levels compared with those elsewhere, this should be resolved by adjustments over a period of years within the interquartile range of annual pay movements.

d. Responsibility for data collection and analysis would be entrusted to an independent Pay Information Board (PIB) of suitably qualified and experienced outside members.



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2. On 4 November the Chancellor of the Exchequer sent you a minute setting out the conclusions of the Ministerial Group on the Megaw Report (MISC 83). The Group was firmly of the view that the Government should accept the Megaw recommendations as a basis for seeking to negotiate a new pay system, although not for "seeking an agreement at any price". Any new pay agreement should, however, be subject to certain safeguards. The Group also wished to explore ways of avoiding reinforcing the concept of an automatic annual pay increase. Officials were to advise on this, and also on the form and timing of a public statement of the Government's attitude to the Megaw recommendations.

3. Mr Scholar replied on your behalf on 8 November asking that further work should be done by officials on the safeguards to which the Chancellor of the Exchequer had referred, and saying that the Ministerial Committee on Economic Strategy should then discuss the issues. The letter of 25 November from the Chancellor's Private Secretary forwards a report by officials on:

- a. safeguards;
- b. avoiding annual pay awards; and
- c. the role of the PIB.

4. The main Civil Service trade unions (Civil and Public Service Association, Society of Civil and Public Servants, and Inland Revenue Staff Federation) are holding special conferences in December to discuss their attitude to Megaw. They are no longer expecting a statement of the Government's views beforehand.

#### MAIN ISSUES

5. The main issues are as follows:

- i. What is the Government's general attitude to the Megaw recommendations?

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ii. What view do Ministers take of the recommendations in the report circulated on 23 November about safeguards and other matters?

iii. How and when should the Government make its attitude public?

General attitude

6. The main question is whether the Committee agrees with the judgement of MISC 83 that a pay system based on the Megaw recommendations would be preferable to free collective bargaining, the only realistic alternative. MISC 83 took the view that it was preferable because, while recognising that the Government would have to accept some limitations on its freedom of manoeuvre, they saw advantage in the limits imposed on the unions' freedom. They also thought that limiting the room for argument would significantly reduce the risk of industrial action.

7. It can be argued that the element of constraint implied in the Megaw system is an undesirable modification of the market approach to pay generally favoured by the Government. On the other hand it is not easy for the Government to bring market pressures to bear in free collective bargaining as effectively as a private sector employer. As experience overseas has shown, Governments find it difficult to be in frequent strife with their own employees and usually have to adopt some settled pay arrangements for them, although these sometimes have to be overridden in times of economic difficulty.

8. Whether or not the Committee agrees that a Megaw system would work better than free collective bargaining, it has to be borne in mind that the Government is not starting from a clean slate. It asked the Megaw Committee to advise on a new pay system and the recommendations accept much of the Government's evidence: the need to take account of market factors, such as recruitment and retention; the importance of affordability; and the need to give less importance to comparability. If the Government were now to conclude that it was unwilling even to negotiate on the basis of the Megaw recommendations, its stance would not be easy to explain either to its own employees or to the public at large.



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9. If the Committee agrees that the Government should negotiate on the basis of Megaw, it is then a question of deciding what the safeguards should be, bearing in mind however the judgement of MISC 83 (paragraph 4 of the Chancellor's minute of 4 November) that "there is obviously no prospect of an agreement which places restrictions on the unions but leaves us totally free".

#### Safeguards

10. The officials' report circulated on 23 November discusses four possible safeguards: termination of the agreement; revision of the agreement; provision to impose a settlement outside the agreed interquartile range; and suspension of the agreement.

#### Termination

11. It is normal for any agreement to provide for its own termination; and there is no reason to suppose that provision for this will create problems. The only question is whether the period of notice should be three months or six months. The period in the previous pay agreement was six months; a shorter period would give greater flexibility for both the Government and the unions. The report by officials concluded that there would not be sufficient advantage for the Government in a shorter period to justify making this a bargaining objective.

#### Revision

12. Provision for amendment by agreement is normal; it appears to raise no problems.

#### Imposition

13. It is recommended in paragraph 24c of the officials' report that the aim in negotiations should be to secure provisions such that "the right of the Government was recognised, on its own initiative, to invite the House of Commons to make a pay award for the Civil Service outside the interquartile limits when it judged national economic circumstances to require this".

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It is recognised that the unions are likely to object strongly to a proposal on these lines. They will see it as a very significant modification of the Megaw recommendations. Unlike proposals relating to termination, suspension or revision of the agreement, this proposal gives a right only to one side, the Government, although the approval of the House of Commons has to be secured, and the right can only be exercised in certain defined circumstances.

14. The Committee will first need to consider whether such a provision is needed and then what form it should take. On the case for a provision MISC 83 took the view (paragraph 7 of the Chancellor's minute of 4 November) that "there will also need to be some form of Parliamentary override on settlements, arbitration awards or both, when economic circumstances require this". The officials' report makes it clear that there is no need for override of an arbitration award so long as the Government ensures that arbitration cannot take place without the Government's agreement. There is also no need for override unless the Government's pay objective is below the interquartile range, ie that the Government wishes Civil Service pay increases to be less than those being granted to 75 per cent of comparable private sector workers. Presumably such circumstances would not arise often. Nevertheless the Committee may feel that in these circumstances the Government ought to have an option other than termination of the agreement, especially if it wishes to act more quickly than would be possible within the notice period for termination.

15. On the form of the provision the main issue is how to define the circumstances where it might be used. The review body formula of "clear and compelling reasons", which has frequently been invoked in respect of the Top Salaries Review Body, might be held to be too wide. The officials' report therefore favours a formula referring to "national economic circumstances", the words used in the Remuneration of Teachers Act 1965 to define the circumstances in which the Government might invite both Houses of Parliament to set aside an arbitral award for the teachers. The Secretary of State for Education and Science may remind the Committee that there has been some discussion in the past as to how restrictive this formula might be. In the context of the teachers the Law Officers have



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advised that it would be difficult for the Government to use this power under the 1965 Act if there have been other pay settlements of similar amounts to which the Government was a party. In the case of the Civil Service pay agreement the formula would be non-statutory. Nevertheless it would be difficult to invoke it if the Government wished to single out Civil Servants for less favourable treatment than other public service groups. Provided that the Committee acknowledge this, such a formula might be the right one.

#### Suspension

16. The officials' report argues against having a provision to suspend the agreement. The main considerations are as follows:

a. It would be hard to deny the unions a parallel right; they would obviously use this right at a time which they judged likely to cause the maximum difficulty to the Government. It might be held that an agreement which both sides are free to ignore whenever they wish is hardly worth making.

b. It is hard to see what benefits the Government would gain from the right to suspend which could not be gained equally well by termination, revision or imposition. There would be no advantage comparable to that which the Government sought in 1981 by suppressing PRU evidence. The PIB will only produce evidence about ranges of pay movements which will be known broadly from other sources. It might in any case be undesirable for the Government to state in advance that it intended to fix Civil Service pay below the lower quartile whatever that might be. But even if the Government did so wish, it could invoke in advance the "imposition" provision outlined above.

17. It would seem therefore that a suspension provision would only be worth considering as an alternative to the imposition provision, if the Committee thought that unacceptable or it proved not to be negotiable.

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#### Avoiding annual pay awards

18. The report by officials points out that under the Megaw system an annual pay award can be avoided where the lower quartile of outside pay movements is zero or less. The question is whether to have a threshold of say one per cent, below which a settlement was regarded as "de minimis" and not implemented. It is difficult to see how such a provision would be negotiable without some arrangements for "catching up" which the Megaw system is designed to avoid. There may also be practical problems when, although the overall increase is below the threshold this covers a spread of different increases for different staff with some getting considerably more than the threshold. The Committee may feel that the right time to deal with this (and the associated issue of having pay awards lasting for more than one year) is when pay movements in the economy generally and the pattern of pay awards have made such a "de minimis" provision both a worthwhile objective and realistically negotiable.

#### Role of PIB

19. Mr Scholar's letter of 8 November asked that the possibility should be studied of charging the proposed PIB with responsibility for taking recruitment and retention data, and job security, into account before reaching the conclusions of its comparability work. The report by officials advises against this on the grounds that it would take the PIB into areas which should be matters for managerial judgement and for negotiation. It might thus tend to constrain further the Government's freedom to secure the level of settlement it wanted. The report does, however, suggest that the PIB might be asked to report on how the relevant factors might be brought to account in the most effective way.

#### Announcements

20. Megaw reported five months ago. It seems highly desirable that the Government should soon give an indication of its attitude to the Committee's recommendations, although this is not now necessary before the unions' December conferences. The Chancellor argued in his minute of 4 November that it is not necessarily right to suppose that any statement should be made



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primarily to Parliament or the media and that it is at least as important for the Government to communicate its views to its own employees. You may wish to invite the Chancellor of the Exchequer to circulate the draft of a Government statement, with proposals on its form and timing.

#### HANDLING

21. You will wish to ask the Chancellor of the Exchequer to introduce the discussion. The Lord Privy Seal will also wish to comment in respect of her responsibility for the Management Personnel Office and you may wish to invite general comments from the Secretary of State for Employment. All those Ministers in charge of Departments and responsible for other public services have an interest and may wish to contribute.

#### CONCLUSIONS

22. You will wish the Committee to reach conclusions on the following:

i. Should the Government accept the Megaw recommendations as a basis for seeking to negotiate a new pay system, subject to any specific safeguards or reservations agreed in discussion?

ii. Does the Committee accept the recommendations in the report by officials circulated with the letter of 23 November on the following possible safeguards:

- a. termination;
- b. revision;
- c. imposition;
- d. suspension.

iii. Does the Committee accept the recommendations on other matters namely:

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e. that there should be no minimum threshold for pay increases, or specific provision for settlements lasting more than one year;

f. that the Government should not seek to extend the role of the Pay Information Board, but should ask it in due course to study the possibilities for bringing market factors into account in the most effective way.

iv. How and when should the Government's decisions be made known?

*PIB  
o  
Market factors  
- do not  
ask them to  
evaluate*

*Pg*

P L GREGSON

30 November 1982