

June 2003

Government Evidence to the Local Government Pay Commission

I Summary

1. The Government attaches the highest priority to reforming and improving public services. The 2002 Spending Review set the framework for service delivery, including delivery of services by local government.
2. Delivering these services requires recruiting and retaining the right number of people with the right skills, motivated to deliver high quality services.
3. Pay has a self-evident role in delivering these service objectives. Pay settlements in the public sector should be consistent with the following principles:
 - **Settlements should support the efficient delivery of improved public services.** To achieve this, settlements must, taken alongside non-pay rewards, facilitate the recruitment and retention of suitable staff, and increase their motivation. However, they must not be unnecessarily high because this would divert money intended to improve public services.
 - **Settlements should be affordable.** Settlements above inflation can only be justified where there are specific recruitment and retention problems, or where the increases will be financed by reform and modernisation changes, including efficiency and productivity savings. Earnings growth in the public sector should be in line with that being experienced in the economy as a whole.
 - **Settlements should give consideration to alternative forms of delivery,** such as e-government initiatives.
 - **Pay systems should promote fair employment practice,** including supporting diversity of staff and equal pay.
 - The Government has put in place a **national framework of fairness,** with the minimum wage and tax credits for the benefit of all sectors in the economy. This minimum income guarantee applies in the same way to all workers.
4. The pay system should act to motivate and incentivise high quality service delivery. Pay systems need to evolve in these directions where they do not already have these characteristics.
5. Pay systems should give employers enough flexibility to tailor their pay and reward packages to meet local recruitment and retention needs.
6. Workforce flexibility, if linked to performance management systems that reward it, can improve performance and tackle recruitment and retention problems, by remodelling the workforce and bringing in new and collaborative approaches across professional boundaries.
7. Employers should understand the importance of, and use, non-pay factors as part of their recruitment and retention strategy.

8. Pay systems should be developed in a way that is consistent with the pay and workforce strategy for local government.
9. The cross-cutting review of the labour market published in November 2002 (and available at: http://www.hm-treasury.gov.uk/Spending_Review/spend_ccr/spend_ccr_labour.cfm) contains a number of recommendations that are relevant to local government.

II Affordability and control of pay settlements

10. It is important that pay settlements are affordable within budgeted resources and do not divert resources away from improving service delivery. In general, public sector pay settlements should reflect current and projected inflation, and any increases above this level should be sufficiently justified in terms of equal pay, recruitment and retention difficulties or modernisation and reform. Furthermore, earnings growth in the public sector should be in line with that in the economy as a whole.
11. Private sector pay settlements averaged 2.8% in the 12 months to February 2003, according to Incomes Data Services (IDS). Over the same period, the percentage increase in prices, as measured by the Retail Prices Index (RPI) was 3.2%. The latest RPI figure, for the 12 months to March is 3.1%.
12. The Government has set the Bank of England an inflation target of 2.5% as measured by RPIX. The Bank has acted quickly and decisively as necessary to keep as close as possible to this target.
13. The Bank of England's latest Inflation Report (February 2002) forecasts RPIX to move above the 2.5% target in the short term due to temporary influences, but then to move steadily back towards the target by the end of 2004.
14. The latest figures for average earnings growth (March 2003) show a headline increase for the economy as a whole of 3.4%

III Local Government Pensions

15. The Local Government Pension Scheme provides a statutory-based final salary pension scheme for local authority employees, and others connected with the sector, in England and Wales under the stewardship of ODPM. It is a vital element in the total remuneration package available to local government's workforce, including provisions for early and ill-health retirement.
16. Membership is open to all employees who contribute 6% of pay; employers on average pay a contribution of 13% of pay. Pension rights in the LGPS are statutorily protected and its pension funds, with a market value of some £75 billion, provide a significant income flow that helps to reduce employers' costs.
17. The advantages to local authority employers and employees of a modern-style Scheme are well recognised. By having a Scheme which is flexible and responsive to the needs of all interests, it can be a powerful HR factor as a means to recruit, retain and motivate staff in their delivery of public services.
18. To ensure that the LGPS continues to provide an efficient and effective benefit framework for its 3 million active and retired members, a Stocktake exercise has concluded that the current benefit package requires adjustments to provide a more responsive and modernised framework for local authority workforces, particularly to reflect the increasing diversity of working patterns, new forms of flexible contracts and more part-time employment. The Scheme has responded well to the challenge of Best Value and transfers by admitting private sector contractors so that employees on transfer can retain their membership of the Scheme.
19. In a broader context, work is in hand to respond to the Department for Work and Pensions Green Paper and Inland Revenue's Green Paper to ensure that the LGPS continues to provide an attractive, reasonable and equitably funded pension level for all its members, having regard to on-going affordability and council tax bills. Plans to ensure the LGPS continues to meet this challenge will be announced shortly.

IV Motivating and incentivising service delivery

20. In the past, it was accepted that public sector staff often progressed automatically up the pay scale each year. Reward was based on time served, not performance or merit. Pay systems were rigid and lacked the flexibility to tackle particular employment challenges, or to motivate and reward service delivery.
21. For the reasons given above, we believe that this needs to change in order to address low performance and reward and incentivise high performance where it has not already done so. This will allow employers to deliver better services and respond effectively to recruitment and retention challenges.
22. Local government job evaluation schemes are often outdated and in some cases based on redundant concepts of certain traditional skills sets. A new emphasis on individual performance and competency, linked to organisational outcomes, will require a new approach to job evaluation – making it ‘fit for purpose’ as part of an overall performance management system.
23. The Government is committed to linking performance and pay explicitly. Several public sector employers have already added performance elements to pay arrangements, and others are currently introducing schemes.
24. There is a wide range of systems being adopted. In central Government **Civil Service** Performance Related Pay has been widely introduced. At the beginning of the period the employees are set performance targets. Some interim evaluation of performance may take place, and at the end of the period employees are assessed and rewarded according to how they performed. More recently these schemes have been adjusted to relate pay increases to demonstrations of competencies (see below)
25. Reward based on **Team Performance** was one of the recommendations from the Makinson report ‘Incentives for Change’. The Makinson model of team based bonus schemes has been piloted in areas of HM Customs and Excise and the Department of Work and Pensions where work is primarily of a team nature, such as in call centres working towards team goals. Team sizes vary widely, from around 100 to several thousand. Stretching performance targets, which are clearly linked to the department’s PSA targets, are agreed with the team. At the end of the period performance against targets is measured, and non-consolidated bonuses are paid accordingly. An independent evaluation of the effect of three team incentive pilots in the **DWP** gave a positive response and the scheme has been subsequently extended.
26. It is too early to judge the Makinson schemes yet. The **Customs and Excise** pilot scheme came to an end in December 2002. There is currently a formal evaluation being conducted to determine the effect of the scheme on the workforce. The results of this evaluation are expected shortly. The University of Bristol is also undertaking some research into the impact of the **team-based bonus** trials in HM Customs and Excise and the Department of Work and Pensions (research expected to be completed in 2004-05, though interim findings should be available in 2003-

- 04). This is likely to be of considerable relevance to local government where much of the work is team based.
27. In **education**, a performance threshold has been introduced for experienced teachers to reward good performance and as a motivation and retention tool. Teachers can apply to have their performance assessed against 8 national standards of effective teaching. If successful, they receive a consolidated pay award and become eligible for further performance-related payments. Although there has been some resistance from the workforce, this is declining as increasing numbers succeed in meeting the threshold requirements. It is too early to have firm evidence of the impact on performance of these schemes.
 28. The DfES has also brought in the 'School Achievement Award'; these are cash awards paid to schools based on school results to be used to fund staff bonuses. The Department is currently evaluating the scheme.
 29. The **Police** have introduced a system of bonuses based on a range of factors such as competencies, performance in difficult situations and the role filled.
 30. The pay progression approach adopted in the Department of Health's 'Agenda for Change' for the **NHS** is competency focused, positioning employees on the pay spine in relation to an evaluation of their job, and embeds progression in a structure of performance management.
 31. The concept of competency-based pay is also likely to be of relevance to local government where a number of functions require specialist skills and abilities. Issues of confidentiality do not lend ODPM to obtain clear examples of the concept of competency-based pay. However, Essex County Council, Cambridgeshire County Council, Alnwick District Council, Solihull Metropolitan Borough Council and Kerrier District Council have been identified by the Employers' Organisation (EO) as going some way towards bringing in competency pay for some staff members. As part of their recommendations, the EO will continue to monitor the effectiveness of these and other schemes. Furthermore, 25% of authorities replying to a survey in 2002 said they had introduced competency-based progression for at least some groups of employees.

V Flexibility at a local level

32. Adequate flexibility in pay at a local level is fundamental to the government's strategy for public sector pay. This was one of the key recommendations of the Government's cross cutting review of the public sector labour market, summarised in Chapter 27 of the Spending Review White Paper. It was underlined by recent budget announcements about the need to introduce a stronger regional and local dimension into public sector pay. Such flexibility allows local managers to address any recruitment and retention challenges by responding to local labour market conditions. Deadweight costs from high settlements in low cost areas can then be avoided. Not all areas or services are faced with recruitment and retention issues to the same extent.
33. Greater workforce flexibility can also help to motivate and improve performance. If given greater delegation, within clear national standards, local managers can take appropriate and timely decisions to manage performance and rewards at the same time as allowing service flexibility to widen choice and accessibility - responding to local needs.
34. To address recruitment and retention problems, local authorities can introduce a 'package' of benefits to employees, in addition to pay or financial incentives. Benefits might include flexibility of working hours and location and opportunities to exchange annualised leave for pay to meet personal circumstances. But to support service delivery directly and longer-term reform, these benefits should be more directly managed to support the organisation's corporate capacity for flexibility and customer responsiveness as well as incentivising the workforce.
35. In schools, the rapid recruitment of support staff in recent years has demonstrated the advantages of flexibility to respond to local needs and circumstances. This will be even more important as we take forward the reform of the school workforce in line with the National Agreement on Raising Standards and Tackling Workload, which was signed on 15 January this year by government, employers and school workforce unions. The national agreement envisages significant increases in the numbers of support staff, the creation of new roles with higher levels of responsibility, and improved opportunities for training, development and career progression. It is essential that the pay system applying to these staff should be sufficiently flexible to ensure that they can be rewarded in a way that reflects their levels of training, skills and responsibilities.
36. There are particular difficulties in the recruitment and retention of staff working in social services. National vacancy rates are estimated to be around 10% for social workers and 15% for occupational Therapists, and are considerably higher in some parts of the country. These are among the highest vacancy rates for any group of local council workers, and threaten to undermine the modernisation programme for social care. The DH is undertaking a national Social Work Recruitment Campaign on behalf of the sector, and from this year has introduced a new Human Resources Development Strategy grant to Councils, but it is for the employers of social care workers to tackle the pay and conditions aspects of the overall strategy to deal with shortages of staff in the personal social services, within the framework of the resources available to them.

37. It follows that any basic national uplift must be modest, in order to allow the additional local and performance elements to be implemented, as appropriate.
38. Local pay and geographically differentiated pay can also give local service providers additional levers to improve performance, address local recruitment and retention problems and take greater account of the degree of challenge facing local services in different authorities.
39. The growing complexity of rules and regulations governing pay and conditions in public services can make the job of interpreting and applying them extremely difficult and time consuming, which can create inflexibilities and inefficiencies. The DfES has invited the STRB to suggest ways in which the School Teachers' Pay and Conditions document can be simplified. It also intends to rationalise the arrangements for recruitment and retention allowances to offer more flexibility and simplicity.
40. Treasury analysis suggests that while there is variation by region in public sector wages (such as higher wages in London and the South East compared to other parts of the country), this variation is much less than that seen in the private sector. One study put the average inner London premium at 25% in the public sector, compared to 35% in the private sector (excluding City).¹ (This relates to the whole pay package and is not simply the effect of London weighting). The evidence also suggests there is relatively little variation between regions outside of London.²
41. Research carried out by the Department for Work and Pensions demonstrates some interesting regional comparisons between private and public sector pay for clerical and secretarial workers between 1990-2001. This shows that there were only 11 counties where the private sector has higher average wages and these are mainly around Greater London and the South West of England (M4 corridor). There were 28 counties where the public sector had higher wages than the private sector, located in the midlands, north of England, Scotland and parts of Wales. (There were 23 counties where there was little or no difference in the average hourly wage between the sectors.) In all locations, the private sector employed considerably more than the public sector. This indicates that there is not a general problem of public sector pay being uncompetitive with private sector pay for these occupations. It does however support the case for greater regional adjustment to public sector pay to reflect local labour market conditions.

¹ Using data from NES 1999/2001; controlled for compositional effects. Source: "London Weighting Advisory Panel Report", GLA, 2002

² Chapter Six, [Cross cutting Review of the Public Sector Labour Market](#), HM Treasury, 2002

VI Use of non-pay factors

42. Pay should be viewed as part of an overall package of benefits that is available to employers as recruitment and retention devices. Pay is not the only motivator - the Audit Commission's 2002 report on recruitment and retention in the public sector showed that many people join the public sector to 'make a difference'; and that pay was listed well behind factors such as bureaucracy, paperwork and workload as reasons why people leave the public sector.
43. We have already started to make real progress in removing controls and freeing up local authorities to respond in innovative ways to address their own problems. At the end of last year we announced a package of measures to give greater freedom and flexibility to authorities - massively reducing the number of plans that we require and reversing the trend on ring fencing of grants. The current Local Government Bill paves the way for even greater freedoms for councils to improve their services and includes freedoms to borrow, to trade, to charge for discretionary services and to retain income from fines. The Innovations Forum is an excellent opportunity to discuss and develop innovative new initiatives so that there is even more flexibility and discretion for Councils. There are also gateways in place to both assess grants and to simplify arrangements for managing 'area based initiatives'. We are also formalising an over-arching local government gateway which will work alongside these. This will ensure that existing commitments on deregulation are delivered and to prevent a build-up of other unnecessary bureaucratic burdens.
44. DfES has introduced an Implementation Review Unit to assess the impact of new and existing policies on the school workforce, and to advise on measures to tackle red tape and bureaucracy. A panel of serving professionals – nine heads, two senior teachers and a bursar will support the IRU.
45. One method of reward less widely used in the Public Sector is **non-financial rewards**. A guide produced by the Cabinet Office (More Than Money, 2001) promotes the use of non-pay rewards specifically related to performance, detailing a number of the advantages of such rewards.
46. Job and role re-design can address the problem of skills scarcity. For example, by isolating the skills set that is hard to recruit and redrawing the professionalism or the job boundary, employers can take advantage of the skills that are more readily available in the market. They can redesign work processes to reduce the impact of the skill scarcity or bring in targeted training programmes to grow the required / scarce skill.

VII Pay and workforce strategy for local government

47. Government needs to have a strategic overview of the capacity needed by local government to deliver its key service priorities in terms of numbers of people, skills, organisational structures, use of new technology. This will complement the strategies for recruitment, retention, working practices and workforce development adopted by local authority employers themselves. Government is currently preparing a strategy and may wish to offer subsidiary evidence later.
48. Pay policies are part of a longer term strategy for building and retaining the workforce capacity and capability needed to deliver services. Short-term responses to immediate pressures should be avoided - they tend to be unsustainable in the longer term, and benefits are often short-lived. Rather, the local government pay and workforce strategy should consider medium and longer term service needs, and the skills that will be essential in the future. The most successful reward policies and interventions are likely to be those that gives local government the means to deal with current and anticipated workforce problems, take advantage of future opportunities, and manage the transition between both.
49. The Government believes that the pay of senior officers in local government should be linked to performance. This is already a key feature of the pay of the senior civil service. In a recent survey by the Society of Local Authority Chief Executives just under a third of local authority Chief Executives who responded had pay which was linked to performance. More commonly, progression up a pay scale depended on length of service. If this is a representative picture, it does not sit well with the need to improve the delivery of key public services. The Government believes that a higher proportion of local authority chief executives should have pay that is based on achieving individual performance targets. There needs to be a clear and public link between the pay offered in order to recruit the correct calibre of staff and the performance expected of the chief executive.
50. There have been several well-publicised instances of chief executive posts being advertised at very high levels of remuneration. Exceptional circumstances might demand exceptional remuneration. But the Government believes that local authorities need to take care to avoid the justifiable exception becoming the unjustifiable norm. Authorities should not offer progressively higher remuneration packages in an effort to “outbid” other authorities when filling senior posts. They should also guard against very high pay for chief executives drawing upwards the remuneration of other senior officers and indeed more junior staff.
51. There is a need to improve the capacity and capability of local government HR specialists and managers for developing local pay systems.
52. Overall there is no formal training and development framework for employer-side pay setting across public services. In addition, competencies have not generally been developed for HR professionals and managers involved in pay and reward policies units, so the grade, skills and knowledge of staff varies markedly across public services. By contrast, the larger unions have a well-developed internal training process (often supported by colleges).

53. (OPSR) The Cabinet Office is working with the Civil Service College to trial a training course for industrial relations managers as a first step to addressing skills deficiencies, and the College is in discussion with the CPD about the possibility of accreditation. The PSEF have agreed to pilot a public service pay club linked to the existing civil service pay club. Consideration should be given to developing modular training programmes for Local Government HR specialists and managers involved in pay and reward policy, and implementing practice; and whether a set of competencies should be developed.

VIII Cross cutting review of the public sector labour market

54. The cross-cutting review of the public sector labour market published by the Treasury in November 2002 reviewed the state of the public sector labour market and made a number of recommendations to increase local pay flexibility, expand the workforce base, present an attractive image of the public sector, expand the opportunities for career development, increase collaboration and sharing of good practice and improve the availability of data, research and analysis. A large number of these recommendations are relevant to local government. The document can be obtained from the internet at: http://www.hm-treasury.gov.uk/Spending_Review/spend_ccr/spend_ccr_labour.cfm or from the public enquiry unit on telephone number: 0207 270 4558.

IX Good employment practice

55. Evidence of good employment practices should be a key factor in selecting a private or voluntary sector partner. Potential partners should show how they will recruit, retain and motivate staff of sufficient quality in order to deliver a high quality service.
56. The Government has taken measures to ensure that staff transferred out from local government as part of a transfer-out of a service are protected. And that staff taken on by a contractor to work beside those transferred staff are also treated fairly. This fits with our view that high quality services depend on a high quality workforce.
57. Procurement exercises should secure fair treatment for staff in line with the policy, but without restricting the flexibility and innovation needed to improve the service. The intention of the measures is to prevent contractors from driving down terms and conditions, at a cost to service quality. It should not lead to fossilisation of a particular set of conditions which may not be the most appropriate for the circumstances.
58. Consideration to be given to developing a set of success criteria to encourage good employment practice when developing robust pay and reward systems. Any pay and reward system must be:
 - supported by sufficient management capacity and training to allow successful implementation
 - must be underpinned by an effective performance management framework.
 - related to the outcomes of the organisation as a whole *and* sufficiently balanced to be relevant to the employee assessed and the behaviour desired.
59. Performance management systems must be fair, robust and workable, at the same time as
 - Being transparent and equitable in operation
 - Valuing contributions from all staff and recognising and rewarding achievement fairly
 - Tapping into local and international and labour markets and skills pools, and making the most of the growing diversity in the population
60. The ODPM have commissioned a business case to explore the feasibility of a Leadership Academy for Local Government. If the Academy is set up, its content must include developing leaders who can:
 - Develop and manage performance management systems that reward good performance, through pay and non-pay rewards
 - Model the behaviours and values that encourage customer focused service delivery
 - Have the competency and vision to set fair, and effective local pay systems