CABINET

CONCLUSIONS of a Meeting of the Cabinet
held at 10 Downing Street on
THURSDAY 10 JULY 1975
at 10.00 am

PRESENT

The Rt Hon Harold Wilson MP
Prime Minister

The Rt Hon Edward Short MP
Lord President of the Council

The Rt Hon Roy Jenkins MP
Secretary of State for the Home Department

The Rt Hon Anthony Crosland MP
Secretary of State for the Environment

The Rt Hon Anthony Wedgwood Benn MP
Secretary of State for Energy

The Rt Hon Barbara Castle MP
Secretary of State for Social Services

The Rt Hon Peter Shore MP
Secretary of State for Trade

The Rt Hon William Ross MP
Secretary of State for Scotland

The Rt Hon Merlyn Rees MP
Secretary of State for Northern Ireland

The Rt Hon Lord Elwyn-Jones
Lord Chancellor

The Rt Hon Denis Healey MP
Chancellor of the Exchequer

The Rt Hon Michael Foot MP
Secretary of State for Employment

The Rt Hon Shirley Williams MP
Secretary of State for Prices and Consumer Protection

The Rt Hon Eric Varley MP
Secretary of State for Industry

The Rt Hon Roy Mason MP
Secretary of State for Defence

The Rt Hon John Morris QC MP
Secretary of State for Wales

The Rt Hon Fred Peart MP
Minister of Agriculture, Fisheries and Food
The Rt Hon Harold Lever MP  
Chancellor of the Duchy of Lancaster
The Rt Hon Fred Mulley MP  
Secretary of State for Education and Science
The Rt Hon Robert Mellish MP  
Parliamentary Secretary, Treasury

The Rt Hon Lord Shepherd  
Lord Privy Seal
The Rt Hon Reginald Prentice MP  
Minister for Overseas Development
The Rt Hon John Silkin MP  
Minister for Planning and Local Government

ALSO PRESENT

The Rt Hon Samuel Silkin QC MP  
Attorney General

SECRETARIAT

Sir John Hunt
Mr P Benner (Item 1)
Mr J A Hamilton (Items 2 and 3)
Mr J A Marshall (Items 2 and 3)

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Uganda
1. The Cabinet were informed of the business to be taken in the House of Commons during the following week.

2. The Cabinet considered a draft of the White Paper "The Attack on Inflation". Their discussion and the conclusions reached are recorded separately.

3. THE PRIME MINISTER informed the Cabinet that a telegram had just been received stating that the Foreign and Commonwealth Secretary had had a meeting with President Amin that morning at which United Kingdom/Ugandan relations and other matters were discussed. President Amin had agreed to release Mr Hills to Mr Callaghan and he would be returning to London with the Secretary of State later in the day. The Cabinet would wish to congratulate the Foreign and Commonwealth Secretary on his successful handling of this extremely difficult situation.

The Cabinet -

Took note, with approval, of the statement by the Prime Minister.

Cabinet Office

10 July 1975
The Cabinet had before them a printed proof of the White Paper on inflation which had been made available shortly before the meeting and which superseded the draft circulated with C(75) 76.

Introducing it THE CHANCELLOR OF THE EXCHEQUER said that the Secretaries of State for Employment and for Prices and Consumer Protection and he had held an intensive series of meetings over the past week with members of the Economic Committee of the Trades Union Congress (TUC) and with representatives of the Confederation of British Industry (CBI). There had been a marked and helpful shift of view by the TUC. At first they had been reluctant to consider any limit for pay increases below 15 per cent, and were also opposed to any legislation in support of a voluntary policy. They had however agreed to a flat rate limit of £6 a week, which was equivalent to a little over 10 per cent, and had also agreed that legislation was needed to enable penal sanctions to be operated through the Price Code; to relieve employers of their contractual obligation to pay more than the proposed limit; and to provide sanctions against individual local authorities through selective use of the Rate Support Grant. He had made it clear to the TUC that the Government also reserved the right to introduce a reserve power to make it an offence for employers to pay over the limit if this were thought necessary even though the TUC would be opposed to this. The CBI had finally accepted the proposed Price Code sanctions, and they had urged that a reserve power was necessary. There were elements in the proposals which they disliked but they had said that if they concluded that the policy eventually announced by the Government would work, they would support it.

The Cabinet then considered the printed proof paragraph by paragraph, and agreed to a number of amendments. The following were the more important points made in this part of their discussion.
The Pay Limit

On paragraph 6 it was noted that the equivalent of 10 per cent for the average adult worker was £5.50 a week; but the agreed flat rate of £6 would not carry through into overtime, and this, taken with the fact that some employers would in fact not be able to afford to pay the £6, meant that the overall effect of a £6 maximum could be equated with 10 per cent. It would however be important to emphasise that £6 was a maximum and not an entitlement. A flat rate had been adopted because a simple percentage, which would give only £3 to the worker on £30 a week, would have been unacceptable to the TUC; while a mixture of flat rate and percentage increase would have been too complicated and made much less impact presentationally. Nevertheless the flat rate created problems. One was that because there were large numbers of low paid workers - who benefitted most from the flat rate - in the clothing, retail distribution and food industries it could have a disproportionate effect on the movement of the Retail Prices Index (RPI). Another was that by compressing differentials and creating anomalies it would increase the problem of re-entry at the end of this phase of the Government's incomes policy.

Expenses

It was noted that there was no reference in paragraph 6 to expenses. It was agreed that expenses should not be affected by the limit, but that this was a point more suitably made in a speech in the subsequent Parliamentary debate.

Upper limit

On paragraph 7 it was agreed that the upper limit for the £6 increase should be £8,500 a year. This would not satisfy fully either the TUC or CBI but was a reasonable compromise which would in particular ease the problem in relation to the power engineers.

Transitional arrangements

On paragraph 8 it was argued that the cut-off date for transitional arrangements should be 1 August instead of 1 September. Admittedly this would involve hardship to certain public employees (including the police, the university teachers and the railway workers) whose later payments would then have to count against the £6 limit, but if the Government were to carry conviction they should allow no exceptions after the date for the introduction of the new policy. Against this it was argued that where public faith was pledged, or where the employees concerned were at the end of the previous pay round, it would be wiser to act with generosity, as long as the transitional provisions were clear and defensible. After further discussion it was agreed to retain the date of 1 September but to allow only
Food subsidies and rents

As regards the alternative paragraphs (34 and 35 or 34A and 35A) dealing with food subsidies and rents THE SECRETARY OF STATE FOR PRICES AND CONSUMER PROTECTION argued that the whole of the £150 million which the Chancellor was prepared to make available in 1976-77 should be devoted to postponing the phasing out of food subsidies. Certain major food price increases were already in the pipeline, including those which would arise from the recent decision to adjust the representative rate for the "Green Pound". The flat rate pay limit would be likely to hit the food and distribution industries more than others, with consequential effects on prices. Other increases would arise from agreements under the Farm Price Review. There was also the prospect of a bad harvest due to the dry summer. The redistributive and egalitarian effect of food subsidies upon incomes was far greater than that of any other form of subsidy. Moreover, rent rebates protected the poorest people from the full impact of the rent increases, which would in any case not be felt until April, whereas the effect upon food subsidies would be felt from September.

Against this THE SECRETARY OF STATE FOR THE ENVIRONMENT argued that the available £150 million should be partly devoted to holding down the rise of £1 a week which would otherwise take place in council rents. This meant an increase next April of 23 per cent which would be highly damaging both politically and economically. People were not very greatly aware of the effect of food subsidies on their shopping bills, whereas the addition of £1 to their rent, coming at a time when local rates would almost certainly suffer an as yet unquantifiable increase, would make a far greater impact. He therefore favoured holding rent increases in line with probable price increases, which would mean a rise of 15 per cent or 60 pence.

After a short discussion, it was agreed that £80 million should be devoted to holding down the increase in council rents, and £70 million to postponing the phasing out of food subsidies.

Employment and Public Expenditure

THE SECRETARY OF STATE FOR ENERGY proposed that paragraphs 38-45 and 47 of the draft White Paper should be deleted since he felt that the draft put forward an economic strategy totally different from that on which the Government had been elected. It would involve real cuts in pay, rising unemployment, and rising prices designed to increase profits in the vain hope that this would
lead to increased investment. It was a recipe for a major slump which would lead to a continuing loss of manufacturing capacity. The TUC favoured an investment-led expansion; but there was nothing in the text referring to the National Enterprise Board, the introduction of planning agreements or the generally interventionist policies of the Government to stimulate more investment. Furthermore, the proposed incomes policy had been represented as an alternative to public expenditure cuts, whereas paragraph 42 foreshadowed further cuts in any case. In his view the strategy was a Conservative one, and would not work.

In discussion, there was no support for the deletion proposed; but a number of amendments were agreed. On public expenditure, it was agreed that the references in paragraph 42 should be amended to make it clear that the review in train was the regular annual procedure, and to ensure that nothing should prejudice the discussion which the Cabinet would shortly have about the level of public expenditure in future years.

It was suggested that a reference to occupational pensions, exempting improvements in them from the pay limit, which had appeared in the Annex to the version attached to C(75) 76, but was not in the printed version, should be restored; but after a brief discussion it was accepted that this would provide an undesirable loophole, particularly for the better paid.

The Cabinet then considered the provisional passage saying that the Government proposed to invite Parliament to enact reserve powers which, if applied in particular cases, would make it illegal for an employer to exceed the pay limit.

THE PRIME MINISTER said that this issue was one upon which the future of the Government could depend. If the White Paper was not seen to be credible and there were a further run on sterling the Government could be forced into much severer policies, including possibly even criminal sanctions against workers to which he had long been, and was still, firmly opposed. He saw the argument for reserve powers as the need to show that there was an effective means of coping with those few employers who settled over the limit, whether out of doctrinaire obstinancy or to poach skilled labour or because they were prepared to buy industrial peace at any price. This was a loophole which the Government needed to be able to close. The reserve powers envisaged could however only be activated by an Affirmative Resolution in Parliament and thereafter
by a specific Order against an individual company. There would be few, if any, cases in practice, since firms would shrink from the publicity which this procedure would involve. He had a strong preference for a policy which was fully agreed with the TUC particularly since the latter had moved further from their original position than had seemed possible. Nevertheless, the size of the minority vote at the TUC General Council the previous day inevitably left doubt about how far they could secure compliance with the agreed limit. The TUC would strongly oppose legal sanctions against workers; but they had accepted the need to legislate in order to relieve employers of their contractual obligations and he believed that they would acquiesce in the proposal for reserve powers against employers even though they would prefer to avoid it. He was as publicly committed against a statutory policy as any other Minister but he believed that the confidence factor made it necessary to take this limited reserve power as part of the legislative package which the TUC had already accepted to be necessary.

THE SECRETARY OF STATE FOR EMPLOYMENT said that, while the Cabinet would necessarily wish to give full weight to the arguments put forward by the Chancellor of the Exchequer at their meeting on 1 July there were other important factors which must be taken into account. In his view the adoption of the proposal to take reserve powers would lead to the destruction of the Government. He had two main reasons for saying this. First, it was important not to underestimate the Parliamentary difficulties. The voluntary policy in the White Paper already needed to be buttressed by legislation eg to provide penal sanctions through the Price Code, to extinguish employers contractual obligations and to take discriminatory powers for the Rate Support Grant. They would lead to a sizable Bill, but the TUC had accepted legislation on these points and there was no escape from it. It would however inevitably feed suspicions that the proposed policy had a strong statutory element. If the reserve powers were added to this it could double the size of the legislation and would certainly involve long and contentious arguments in the House of Commons. There would be strong objections from the Government’s own supporters; and the Opposition would be able to use the position to its own advantage. In the resulting Parliamentary shambles, the Government’s position would be seen as very weak and this would be just as damaging for sterling as the absence of a reserve power. Secondly, and concurrently with the Parliamentary troubles, there would be great difficulties with the trade union movement. He agreed that the vote at the previous day’s TUC General Council had been disappointing, but the TUC document had been better than we had dared expect and this in itself must have lost some votes. There would probably now be a passionate debate
within the trade union movement to influence the vote at the meeting of Congress on 1 September. The TUC leaders who had done most to help the Government hitherto would be greatly hampered in this debate if reserve powers were now taken against their advice and wishes. This in itself could lead to an adverse vote at the Congress meeting which could in turn be very bad for foreign confidence. The truth was that it was not possible to run an effective incomes policy without the support of the trade union movement. The Government and the trade unions should move in step and he pleaded with Cabinet not to agree to reserve powers.

THE CHANCELLOR OF THE EXCHEQUER said that the decision facing Cabinet was not an easy one; but he felt that he had a duty to recommend the adoption of the reserve powers proposal. The TUC policy for pay coincided almost completely with that of the Government; but the problem of compliance remained and the credibility of the policy had suffered a setback from the previous day's TUC General Council vote. In his view there were three reasons for adopting the reserve powers. First, it was essential to be able to assure the workers who settled early in the coming pay round that, if they conformed with the policy, they would not be overtaken by others who came later. The sanction through the Price Code was unlikely to be effective in the case of capital-intensive firms, but if it were made illegal for employers to pay more than the limit, this would - without actually invoking the powers - enormously increase the degree of compliance. Secondly, while he acknowledged the Parliamentary difficulties, he believed that there was overwhelming public support, both in the country and in Parliament itself, for a policy backed by reserve powers. It was better to take the powers now rather than have to ask for legislation later when the mood might have changed. Thirdly, it was absolutely essential that the White Paper should carry conviction immediately to foreign holders of sterling. The general expectation was that reserve powers would be included in the policy, and if they were not there was a danger of an even more serious run on sterling. This situation might be impossible to retrieve and could lead to a collapse both of the currency and the Government. He recognised that the proposal would create great difficulties for the trade union movement, and particularly for those who had been most helpful in shifting opinion within the TUC in the previous fortnight. But he believed that they would still fight to make the policy work and he believed that without the reserve powers the policy would not be a credible one.

There was a general recognition that neither of the alternative courses was easy, and that each presented its own danger and difficulties. The Cabinet had to weigh the relative cost in terms of trade union goodwill against the risk of a run on the pound. The essential thing to avoid was a White Paper which did not carry
conviction and which then led to a fall in the exchange rate compelling the adoption of even sterner policies than those now in contemplation. It would in any case be a mistake to put too much emphasis on the reserve powers. In terms of anti-inflation policy, they were of little significance compared with the importance of the Government’s willingness to stand up to strikes. It should be stressed that the main weight of the Government’s policy rested on the financial sanctions.

In further discussion the following main points were made:

a. The previous day’s TUC General Council vote was a serious disappointment, particularly since a year earlier the Council had voted unanimously in favour of much less severe guidelines which had subsequently been ignored by many unions. If the Council were divided over severer guidelines, the prospect of compliance with them must be much less even than last year. Against this it was argued that in 1974 the TUC had been voting on some general and rather ideal guidelines, whereas this year they had been dealing with far more practical and detailed suggestions. It was remarkable and significant that these had still won a majority vote.

b. It was fallacious to suggest that the reserve powers proposed would operate only against employers. Even though trade unions would be absolved from any liability to be charged with conspiracy, the truth was that in the present economic climate an employer would only pay an increase above the limit under pressure from a trade union. In that situation if the Government went to Parliament to obtain an Order against that employer, they would be effectively seeking to exercise a sanction against the workers. Furthermore, they would be seeking to impose a penalty upon an employer who was by definition in a position of great difficulty. It must be doubtful whether the House of Commons would in fact approve such an Order.

c. The political problem would be a continuing one. Even if the Bill were passed, there would be further crises, and the Parliamentary Labour Party would become broken and dispirited. The Government would then become dependent upon the capricious support of the Conservatives. The real test of a voluntary policy would come when a major union sought to use its muscle in defiance, and at that point the Government would need the strong support of the TUC. This consideration overrode the more immediate arguments in favour of taking reserve powers.
d. The reserve powers were in any case a transparent bluff. They meant that an employer could be driven into bankruptcy by the action of a powerful union; and it might be that when a case were brought against an employer he would be able to plead force majeure, in which case the credibility of the power would rapidly be undermined. Even if he could not effectively make this plea and were fined, the fine would have to be both large and continuous to make the sanction work. This was hardly likely to be an effective policy.

e. If the operation of reserve powers was likely to be both limited and unfair, this would become apparent in the Committee stage debate in the House of Commons (where the Government might well face defeat) and would hardly impress our overseas holders of sterling. The truth was that any policy could only succeed by a consensus.

f. On the other hand it was very difficult for members of the Cabinet other than the Chancellor to assess the likely effect on foreign confidence of a policy with or without reserve powers. Great weight had therefore to be attached to his judgment.

In further discussion it was suggested that one course which might ease the dilemma facing Ministers would be to refrain from including the reserve powers in the Bill which would be introduced following the White Paper and instead to include in the White Paper a pledge that the Government was determined to ensure success and a statement that the Government had a further Bill in reserve, which would be introduced at once if it were needed, to compel observance of the pay limit by all employers. In considering this proposal, it was argued that there was a risk that, if the reserve powers were not included in the first Bill, it would be difficult to carry conviction that the Government would in fact face up to taking statutory powers later. It would also be a mistake to think that reserve powers would have little effect upon the course of events - on the contrary, their existence would be likely to have a considerable influence, which was one reason why the CBI were in favour of them. Nevertheless, the battery of sanctions, including some legislation, with which the voluntary policy would be supported was impressive, and the Government had achieved a surprising degree of support and understanding from the Unions. It might therefore just be possible to hold the exchange rate with the intermediate proposal which had been made.

THE PRIME MINISTER, summing up the discussion, said that the Cabinet had to reach a very grave judgment, and they should not underestimate the seriousness of the situation they would face if the White Paper failed to carry conviction and a further serious run on the pound developed. The distinction which had been drawn
between taking reserve powers and holding legislation in reserve was however a subtle and significant one. The latter course would do much to ensure whole-hearted trade union support for the new policy; and the Chancellor of the Exchequer had indicated that he thought it should just go sufficiently far to reassure overseas opinion provided the statement about the Government's readiness to introduce the further legislation, if needed, were made in sufficiently robust terms and provided the White Paper as a whole appeared to carry conviction at home. It seemed clear that the existing balance of opinion in the Cabinet was against the inclusion of reserve powers in the immediate legislation and in favour of a clear statement in the White Paper that the Government had a further Bill ready for presentation and enactment if this became necessary. He proposed that he and the three Ministers who had conducted the negotiations with the TUC and CBI should meet to consider the redrafting of the relevant paragraphs of the White Paper which would be necessary to give effect to this consensus. They would also be seeing the TUC and CBI later in the afternoon. If necessary he would ask the Cabinet to meet again following these meetings.

The Cabinet -

Took note, with approval, of the Prime Minister's summing up of their discussion.

Cabinet Office

11 July 1975