



18 October 2010

Rt Hon Danny Alexander MP
Chief Secretary to the Treasury
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

Dear Chief Secretary

INDEXATION OF PUBLIC SERVICE PENSIONS

Thank you for your letter of 14 October 2010.

As I said in my earlier letter, we consider that the Government is in breach of assurances given by both Conservative and Liberal Democrat spokesmen immediately prior to the General Election; contractual obligations freely entered into by the Government as employer; and the Human Rights Act 1998 and find your explanation that the assurances provided prior to the General Election only protected the past increases based on RPI somewhat bizarre. What would have been the point of the Alliance pressing for assurances regarding increases already made, which are obviously protected by law, and are you really suggesting that the assurances given were not intended to assure Civil Service pensioners that the Coalition partners would protect arrangements for future increases to be based on RPI? I'm afraid that your attempts to suggest that the pre-Election assurances only protected past increases based on RPI will only provoke further consternation and anger amongst pensioners! The Alliance will be considering further legal advice on these matters and will be writing to you again.

The purpose of this letter is to set out in rather more detail why we consider that the Government's proposed move to CPI is in breach of the Secretary of State's obligation under Section 59 of the Social Security Pensions Act 1975 and Section 151 of the Social Security Administration Act 1992 to increase pensions in line with the "general level of prices". The CPI does **not** provide "a more appropriate measure of benefits and pension recipients' inflation experiences than RPI", nor does it meet the legal requirement to reflect the "general level of prices."

There are two reasons why the CPI consistently produces a lower measure of inflation than does the RPI:

- (a) Its narrower coverage - mainly because it omits owner-occupied housing costs (of which mortgage interest payments are an important but not the only element),
- (b) The 'formula effect', because, given the same price data, the two indices are put together in different ways

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The relevant legislation requires the Secretary of State to uprate various benefits, so that they retain their value relative to 'the general level of prices'. Although he has discretion as to how to measure the increase in prices, this discretion does not extend to choosing an index that deliberately excludes a significant element of living costs, since this would not then be a measure of the general level of prices.

The choice of inflation index involves technical statistical issues. In making a choice of index, the Secretary of State would be expected to consult statistical experts and listen to their advice, even if the final decision was his alone. Deliberately not to do so argues that the choice was made on extraneous grounds and was not a good faith choice of an appropriate index to uprate benefits.

On 06 September 2010, Sir Michael Scholar, Chair of the UK Statistics Authority, wrote to one of our members, saying that his understanding was that the National Statistician had not been asked for advice about the switch from RPI to CPI. The UK Statistics Authority is an independent body operating at arm's length from Government as a non-ministerial department, directly accountable to Parliament. It was established on 1 April 2008 by the Statistics and Registration Service Act 2007. Its statutory objective is to promote and safeguard the production and publication of official statistics that serve the public good. It is also required to promote and safeguard the quality and comprehensiveness of official statistics and ensure good practice in relation to official statistics. Therefore, it seems incredible to us that the Government chose not to seek advice from the authority before embarking upon such a radical change, which will adversely affect not only public service pensioners but, also, state pensioners and benefits claimants.

With this background, I refer you to the attached correspondence between Professor David Hand, President of The Royal Statistical Society, and Sir Michael Scholar KCB, Chair of the UK Statistics Authority.

You will see that Sir Michael says - *We believe that the CPI should become the primary measure of consumer price inflation but only when the inclusion in the index of owner occupiers' housing costs has been achieved.* It is pretty clear from this that the UK Statistics Authority does not think that the CPI, without housing costs, is the best currently available measure of consumer price inflation.

You will see that Section 2 of Professor Hand's letter points out the statistical difficulties with both RPI and CPI. He states that - *We consider it highly unsatisfactory that a difference in statistical treatment should generate such a substantial difference in the two indices; we are not aware of any other country where the difference is as great.* He goes on to suggest that this difference might be due, in part, to - *the UK giving greater latitude to price collectors as to the type of product they collect for certain goods (since the extent of the difference between the average of relatives and the geometric mean increases with the heterogeneity of the relatives).* This seems to imply that the methodology for collecting prices that the UK has used hitherto has been appropriate for calculating the RPI but is less appropriate for calculating the CPI. Sir Michael does not respond to this point directly but mentions that - *The Authority is also assessing the set of inflation indicators against the Code of Practice for Official Statistics. Our findings will be set out, as usual, in a published Assessment Report.*

It appears to us that the Government is not yet in a position to judge that CPI, as it currently stands, is "a more appropriate measure of benefits and pension recipients' inflation experiences than RPI" nor does it meet the requirements of primary legislation. Therefore, we ask you to

stay your hand on this important issue until the statistical methodology has been revised and interested parties have been given the opportunity to comment.

We would welcome your further comments on these important issues and I look forward to hearing from you.

I am copying this letter to the Pensions Minister, Steve Webb MP, Anne Begg MP, as the Chair of the Select Committee on Work & Pensions, Andrew Morris at PSPC and, in view of the wider public interest, to the press.

Yours sincerely

A handwritten signature in black ink, appearing to be 'John Amos', written in a cursive style.

John Amos
Deputy General Secretary