

PO-CH/NL/0305

PART A

Part A

**SECRET**

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Begins : 21/9/87.

COMMERCIAL - IN - CONFIDENCE

Ends : 24/12/87.

PO -CH /NL/0305

PART A

Chancellor's (Lawson's) Papers:

THE NATIONAL NUCLEAR  
CORPORATION SELLING OFF  
OF SHARES

Selling of Shares

PO -CH /NL/0305

PART A

DD'S : 25 Year

*Phillips*

25/10/95



SECRETARY OF STATE FOR ENERGY

THAMES HOUSE SOUTH  
MILLBANK LONDON SW1P 4QJ

01 211 6402

The Rt Hon John Major MP  
Chief Secretary to  
The Treasury  
Treasury Chambers  
Parliament Street  
LONDON  
SW1P 3AG

SECRETARY	
21 SEP 1987	
<i>Mr M L Williams</i>	
<i>EXEST - Mr Butler</i>	
<i>Mr Monck Mr Burgess</i>	
<i>Mr Moore Mr Turnbull</i>	
<i>Mrs Diggle Mr Tyrrie Mr Call</i>	

21 September 1987

*Dear John,*

**NATIONAL NUCLEAR CORPORATION (NNC): GEC'S 'PUT' OPTION**

GEC, which is the major industrial shareholder in NNC, has an option to 'put' its shareholding onto the UKAEA. This option expires at the end of this month, and I am writing to seek your approval to the extension of the option for a year.

We are of course committed to selling the UKAEA's 35% shareholding in NNC at the earliest opportunity consistent with obtaining a fair price for the shareholding. The electricity supply industry is by far NNC's largest customer. Whilst we are deciding the most appropriate structure for the privatised esi, considerable uncertainty will surround the prospects of NNC, such that we could not hope to obtain a fair price for the shares.

We should aim in the meantime to keep all potential purchasers of the shares in play. GEC have a central role in the company at present and it would be damaging to our prospects of selling the shares if they were to pull out now - as they might if we did not renew the put option. Such a decision by GEC would also of course mean a call on public funds (some £10 million-£12 million) and bring NNC into the public sector. I am sure that the only sensible thing to do at present is to renew the option for a year. I should be grateful for your agreement.

*James Lee,  
Lord*

**CECIL PARKINSON**

COMMERCIAL IN CONFIDENCE

From: P C Diggle  
23 September 1987

1. MR M L ~~WILLIAMS~~ *Agreed in draft*  
2. CHIEF SECRETARY

*LST  
2 PWP  
PJP*

cc Chancellor  
FST  
Mr FER Butler  
Mr Monck  
Mr Turnbull  
Mr Beastall  
Mr Tyrie  
Mr Call

**NNC: GEC PUT OPTION**

This submission recommends, reluctantly, that you should agree Mr Parkinson's proposal to extend GEC's put option on its NNC shareholding. There is little realistic alternative. It means continuing a contingent liability.

The current position

2. The National Nuclear Corporation (NNC) is a construction company specialising in nuclear power stations. It was formed by fusion of the nuclear construction interests of several companies and is owned by a consortium of GEC (30%), AEA (35%) and British Nuclear Associates (35%). In turn BNA is a loose grouping of Babcock, Taylor Woodrow, MacAlpine, NEI and others. The various partners are jealous of each others' interests. In practice the company is rather poorly run by representatives seconded from its various shareholders.
3. Since the amalgamation GEC has insisted on maintaining a right to sell its shareholding in NNC to the government should it wish to do so. These are the only terms upon which GEC has been willing to maintain its shareholding. Each time this put option has been close to expiry, GEC has threatened to exercise the put option if it was not renewed. So far we have not managed to find a way out of this box, though we have explored - fruitlessly - the option of charging GEC for the option.
4. GEC of course is in a strong bargaining position. If the put option were called, the government's shareholding would rise to 65%, suggesting that NNC should be classified to the public sector. The only way out of this problem would be to sell the AEA shareholding.

Sale of AEA's NNC shares

5. During the protracted public enquiry on the PWR nuclear power station at Sizewell B, it would have been improper to sell the AEA shareholding. The Secretary of State could have been held to have a material interest in making a favourable decision on Sizewell. We therefore pressed DEN officials to begin proceedings for sale of the shareholding as soon as the Sizewell decision was made in January.
6. In practice selling the shares is non-trivial. They are worth perhaps #15m, depending on the view taken about the volume and quality of future business likely to fall to the company. The

company is not quoted and any significant disposal would have to take place with the concurrence of the other shareholders. Despite genuine efforts, this proved impossible in the period between the Sizewell decision and the election.

7. Since the election DEN officials have pointed to the commitment to electricity privatisation to explain why it has not been possible to resume negotiations. Unfortunately, this is correct. Without incentives, a privatised electricity industry would not choose nuclear power stations on economic grounds alone, throwing doubt on NNC's prospects after Sizewell. It is reasonable to conclude that the AEA's shares would be saleable only at a severe discount, if at all, without some assurance about the continuation of the nuclear industry. We are not yet ready to give that, still yet indicate the form it might take.

#### The proposal

8. Mr Parkinson therefore proposes to renew GEC's put option when it falls due at the end of the month.

9. There is no doubt that, as before, GEC would insist on forcing the sale of their shares to the government if we hung back. Calling their bluff could be an expensive and probably irreversible mistake. We therefore agree that renewal is the least unsatisfactory option. It means continuing to accept a contingent liability of some #10-12m. At least the extension is only for a year, not two as has happened before.

#### Next steps

10. In discussion with Mr Parkinson's officials we have emphasised the desirability of divesting the AEA of its NNC shareholding as soon as it is feasible. They believe it should be possible to sweep away the put option in the process of disposal, since it would almost certainly be necessary to rewrite the Articles of Association of NNC anyway.

11. Decisions on electricity privatisation are likely to be announced next March, in line with the Chequers decision last week. Allowing a few months for negotiation, it should be possible to complete the sale of AEA's shares in NNC during the summer of 1988. So it is reasonable to allow a one year extension of the put option. Less could leave too short a window between the privatisation decisions and its expiry.

#### Recommendation

12. Despite the unsatisfactory extension of a contingent liability, we advise you to agree the proposed continuation of GEC's put option on the AEA's NNC shares for a further year. A draft letter is attached.

*P C Diggle*

P C Diggle

Draft letter to:

Rt. Hon. Cecil Parkinson MP,  
Secretary of State for Energy,  
Department of Energy  
Thames House South,  
Millbank  
SW1P 4QJ

**NNC: GEC'S PUT OPTION**

Thank you for your letter of 21 September.

2. I am grateful for your commitment to selling the AEA's shareholding in NNC. It is an anachronism that this shareholding remains in the public sector, and hardly conducive to maximising the efficiency of the nuclear industry. I therefore very much hope that we can work toward its early disposal.

3. For the time being, however, I quite see that any attempt at a sale would inevitably generate indefensibly low proceeds so long as the future structure of the electricity industry remains undecided. I am therefore prepared to go along with your proposal to extend GEC's put option. I hope we can return to the question of selling the AEA's shares in good time to avoid any possibility of further renewal.

JOHN MAJOR

SECRET



SECRETARY OF STATE FOR ENERGY

THAMES HOUSE SOUTH  
MILLBANK LONDON SW1P 4QJ

01 211 6402

Copy 1 of 8  
Bf with advice of 7/12

CH/EXCHEQUER	
REC.	30 NOV 1987
ACTION	Mrs Diggle
COPIES TO	CST FSD Sir P Middleton Mr Monck Mr RTH Moore Mr M Williams

The Rt Hon Nigel Lawson MP  
Chancellor of the Exchequer  
Treasury Chambers  
Parliament Street  
LONDON  
SW1P 3AG

30 November 1987

Be chad

*Dear Nigel*

**NATIONAL NUCLEAR CORPORATION (NNC)**

I am writing to let you know of an approach from Lord Weinstock to buy the UKAEA's 35% shareholding in NNC.

NNC's nuclear engineers and project managers comprise an important national resource. The company has a large fund of experience on the Advanced Gas-Cooled Reactor (AGR) and it has been seen as the natural vehicle through which Pressurised Water Reactor (PWR) technology should pass from Westinghouse to the UK. It is not however in the lead on Sizewell B, where its role on the nuclear island is that of a sub-contractor to Westinghouse.

With attention turning to the arrangements for Hinkley Point C, I believe it is important that NNC should be put on a better footing in good time before the opening of that Inquiry, not least in view of the attention given at the Sizewell Inquiry to the effectiveness of nuclear project management arrangements in the UK.

The heart of NNC's problem is its complicated shareholding structure which leaves none of the industrial shareholders firmly in charge and with the Government's shareholding limiting the company's commercial freedom.

The key to this problem is the General Electricity Company (GEC). It was intended at the inception of NNC that GEC should have the dominant role. With the long delay in launching the PWR in this country, GEC saw that NNC's commercial prospects would be limited and reduced its shareholding from 50% to 30%. It retained its powerful position over the other industrial shareholders (which include Babcock and NEI) as originally agreed with Government. No settlement of NNC's industrial shareholding is possible without GEC's agreement. GEC also has pre-emption rights on the UKAEA's shares in the event of their being offered for sale.

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We need to consider the approach from Lord Weinstock against this background. He has told me that he is prepared to put strong managerial and financial resources into NNC. The approach has been strongly commended to me by the CEGB, the UKAEA and the present Chairman of NNC, Sir Frank Gibb. On this basis I am inclined to welcome Lord Weinstock's approach.

There are however other industrial interests involved, notably Babcock (now part of FKI Electrical) and Northern Engineering Industries (NEI) which both have a substantial stake in NNC through a holding company British Nuclear Associates (BNA). I have not yet taken soundings amongst all these parties; in particular I shall be seeing John King, who is Chairman of BNA, later this week. I will not be able to form a considered view and a firm recommendation until I have completed these consultations. I hope to be in a position to do so within the next two weeks.

If in the event we do decide that Lord Weinstock's approach represents the best way forward for NNC, we shall need to consider carefully how the sale should be presented.

I have assured Lord Weinstock that his approach will be kept close within Government. Because of the sensitivity I am copying this letter only to the Prime Minister and David Young and I should be grateful if it could be handled in close confidence.

*Cecil Parkinson*  
CECIL PARKINSON

SECRET



PWP

SECRET

*Wm*  
3/2

From: P C Diggle  
3 December 1987

- 1. MR M L WILLIAMS
- 2. CHIEF SECRETARY

- cc Chancellor
- FST
- Mr Anson
- Mr Monck
- Mr Moore
- Mr Burgner
- Mrs Brown
- Mr Lyne
- Mr Call

NATIONAL NUCLEAR CORPORATION

Mr Parkinson's letter of 30 November seeks approval to sell the AEA's shares in NNC to GEC, with probable proceeds of some #10m in 1988-89. This is an excellent offer to which we think you should agree.

2. NNC is a shell company which constructs the nuclear islands of nuclear power stations. The current shareholdings in NNC are:

GEC	30%
AEA	35%
BNA	35%

(British Nuclear Associates is a loose consortium of construction companies).

3. NNC was formed in 1973 when the CEGB intended to build PWRs. When that plan was abandoned, the industrial shareholders lost interest in the business, with the result that the company is undercapitalised and therefore finds itself unable to compete on normal commercial terms for nuclear construction business. There have been uncomfortable consequences of this unease:

- (a) as the price of continuing its shareholding, GEC has insisted since 1976 on a put option on its NNC shares. So we have been exposed to a contingent liability of some #10-15m that we might have to purchase NNC shares, taking the company into the public sector;
- (b) NNC has not had the resources to design and build turnkey nuclear contracts for CEGB and SSEB. So the ESI has had to manage its projects more directly than would be desirable, with appalling consequences for their cost and timeliness;
- (c) a specific manifestation of (b) is that we have been coerced into providing guarantees for NNC's role in building Sizewell, with a potential risk of some #16m.

4. You will recall that, in agreeing to (c), you urged Mr Parkinson to do his best to sell the AEA's shareholding in NNC. The plan was to minimise our exposure to the contingent liability (c) by eliminating both (a) and (c) in the sale. His officials were discouraging about this, fearing that it might be improper to approach potential purchasers while electricity privatisation was being actively considered. But Lord Weinstock's offer is spontaneous and can therefore be followed up with propriety.

5. Mr Parkinson intends that the sale should sever all connection with NNC, ie that no contingent liabilities such as (a) or (c) should remain. Nor is it intended to offer under the counter promises about future contracts for further PWR power station orders after Sizewell. These restrictions could mean accepting a discount on the value of the shares, whose book value is probably about #15m. This would have to be thrashed out in negotiation on the strength of professional advisers' views on valuation. There is a valuation procedure in the company's Articles in case of dispute.

6. Mr Parkinson knows full well from your letter of 29 September that you will have no difficulty with the proposal to sell the AEA's shareholding. The real purpose of his letter is to get Lord Young on board. He might object that sale to GEC would create a monopoly in supplying nuclear construction services to CEGB or its successors. But:

- that monopoly in effect already exists in that NNC is the only British company in the nuclear construction business;
- the real competition is international, where so far there has been no British player because NNC is financially so weak;
- under NNC's Articles, GEC would have preemption rights anyway if a sale to any third party were contemplated. So taking up this offer would simply mean that we would get a better price.

7. We therefore **recommend** that you agree to Mr Parkinson's proposal, which should free us from two contingent liabilities and provide modest sale proceeds of perhaps #10m. We expect that it will take until early in 1988-89 to arrange the sale, but there is a small possibility that it might take place in this financial year. A draft letter is attached.

*P C Diggle*

P C Diggle

CONFIDENTIAL

Draft letter to:

Rt. Hon. Cecil Parkinson PC MP,  
Secretary of State for Energy  
Department of Energy  
Thames House South  
Millbank  
LONDON SW1P 4QJ

November 1987

**NNC**

Thank you for your letter of 30 November.

2. It is excellent news that GEC have come forward with an offer to buy the AEA's shareholding. As you know, I am anxious to escape the contingent liabilities associated with the AEA's shareholding.

3. The sale should also enable our civil nuclear industry to compete <sup>more</sup> effectively on the international market for power station construction. It will make much more sense for the CEGB's privatised successor(s) to deal with a properly capitalised and independent British company.

3. I am content to leave it to you to decide how best to carry this initiative forward. I am sure my officials will give yours all the help they can in dealing with the various sensitive issues, for example valuation and presentation, which are sure to arise.

JOHN MAJOR

cc - CX, RST, Mr Butler  
Mr Mack, Mr Turnour  
Mr Beasdale, Mr Treac  
Mr Can



Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Cecil Parkinson MP  
Secretary of State for Energy  
Department of Energy  
Thames House South  
Millbank  
London  
SW1P 4QJ

*Dear Cecil,*

29 September 1987

**NNC: GEC'S PUT OPTION**

Thank you for your letter of 21 September.

I am grateful for your commitment to selling the AEA's shareholding in NNC. It is an anachronism that this shareholding remains in the public sector, and hardly conducive to maximising the efficiency of the nuclear industry. I therefore very much hope that we can work toward its early disposal.

For the time being, however, I quite see that any attempt at a sale would inevitably generate indefensibly low proceeds so long as the future structure of the electricity industry remains undecided. I am therefore prepared to go along with your proposal to extend GEC's put option. I hope we can return to the question of selling the AEA's shares in good time to avoid any possibility of further renewal.

*Yours Ever,*  
*John*

JOHN MAJOR

CONFIDENTIAL



CC-EX-15T  
Mr. Anson, Mr. Major  
Mr. Moore, Mr. Bueger  
Mrs. Brown, Mrs. Diggle  
Mr. M. Williams, Mr. Lines

Treasury Chambers, Parliament Street, SW1P 3AG Mr. Call

The Rt Hon Cecil Parkinson PC MP  
Secretary of State for Energy  
Department of Energy  
Thames House South  
Millbank  
London  
SW1P 4QJ

pmp

7 December 1987

Dear Secretary of State,

NNC

Thank you for your letter of 30 November.

It is excellent news that GEC have come forward with an offer to buy the AEA's shareholding. As you know, I am anxious to escape the contingent liabilities associated with the AEA's shareholding.

The sale should also enable our civil nuclear industry to compete more effectively on the international market for power station construction. It will make much more sense for the CEGB's privatised successor(s) to deal with a properly capitalised and independent British company.

I am content to leave it to you to decide how best to carry this initiative forward. I am sure my officials will give yours all the help they can in dealing with the various sensitive issues, for example valuation and presentation, which are sure to arise.

Yours sincerely,

John Major

pp JOHN MAJOR

(Approved by the Chief Secretary  
and signed in his absence).



SECRETARY OF STATE FOR ENERGY  
THAMES HOUSE SOUTH  
MILLBANK LONDON SW1P 4QJ

01 211 6402

CH/EXCHEQUER	
REC.	30 DEC 1987 <i>sch</i>
ACTION	CST
COPIES TO	

The Rt Hon Malcolm Rifkind  
Secretary of State for Scotland  
Dover House  
Whitehall  
LONDON  
SW1A 2AU

23 December 1987

*Dear Secretary of State,*

**NATIONAL NUCLEAR CORPORATION (NNC)**

I have recently been approached by Lord Weinstock with a tentative proposal to buy the UKAEA's 35% shareholding in NNC. (As you may know, GEC has pre-emption rights over the UKAEA's shares and other entrenched rights over the conduct of the company's business.)

I have assured Lord Weinstock that we will keep knowledge of his approach to the smallest possible number of people. Many different organisations have interests in NNC and I have been undertaking a preliminary round of consultations. So far I have spoken to Lord King (who is Chairman of British Nuclear Associates Ltd, the other shareholder in NNC, which is a group of industrial companies with an interest in the construction of nuclear power stations), Sir Frank Gibb (Chairman of NNC), John Collier (Chairman of UKAEA) and Lord Marshall.

I am conscious that the South of Scotland Electricity Board (SSEB) is a major customer of NNC and may well have views on a proposal to dispose of the UKAEA's shareholding. I am proposing to have a word with Donald Miller, but before doing so, I wanted you to know of Lord Weinstock's proposal. In particular, I am sure you will want to know of assurances which he has given to me that if GEC acquires control of NNC, it will, subject to the appropriate commercial terms and conditions ensure that NNC meets its obligations with regard to the AGR programme, including the Heysham and Torness nuclear power stations presently under construction. GEC has also undertaken that it would maintain the open purchasing policy of NNC and, in particular, the awards of contracts on merit without any preferential treatment.

I am copying this to the Prime Minister, Nigel Lawson and David Young.

*Yours sincerely*  
*Stuart Brand*

CECIL PARKINSON

CONFIDENTIAL

*(Approved by the Secretary of State & signed in his absence.)*

CONFIDENTIAL

From: P C Diggle  
24 December 1987

1. MR M L WILLIAMS

*W*  
24/12

cc Chancellor  
Chief Secretary  
Sir P Middleton  
Mr Anson  
Mr Monck  
Mr Moore  
Mrs Brown  
Mr Lyne  
Mr Call

2. FINANCIAL SECRETARY

#### SALE OF SHARES IN NNC

X | This note is for information only. It reports progress on the proposed sale of the AEA's shares in the National Nuclear Corporation (NNC), to which the Chief Secretary agreed in his letter of 7 December to Mr Parkinson.

2. Earlier this week DEN officials held a beauty contest to select a merchant bank for advice on the sale. The field was limited because we could not engage any adviser to the other shareholders in NNC. The contestants were Barclays de Zoete Wedd (BZW), County NatWest and Barings. The job could not be advertised because of the need for commercial confidentiality, which each of the banks undertook to respect.

3. Barings emerged as the clear best buy. Although County offered a good written presentation, their team were lightweight at the interview. BZW had nothing to recommend them: they had simply not thought through what the work would entail. By contrast Barings put together a reasonably coherent document, supplemented by a short slide show at the beauty contest. Most important of all, they showed a sensitive grasp of the difficult negotiation ahead with GEC and the other shareholders.

4. We were also able to negotiate an acceptable fee, about half of what Barings originally asked. It has an incentive structure: we will pay hourly rates up to a maximum of #100k, plus 2% of the difference between the sale price and the equivalent asset value of the shares, if any. This means that the fee could double to #200k if we manage to sell for #15m against an asset value for the shares of some #10m. Given the circumstances of the sale, we think any excess above asset value sufficiently unlikely that Barings will have earned a bonus if they succeed in negotiating it

5. It is pleasing to be able to give this piece of minor privatisation work to Barings, who have not previously been engaged by the government for privatisation work. It shows that we really are willing to cast the net wider if suitable candidates are available.

6. DEN are also arranging to obtain legal advice from Freshfields. There would have been little point in arranging a competition as the other major corporate lawyers were all already committed to the other shareholders.

7. For the moment we do not envisage any need for reporting accountants. For a private sale such as this, where so much will depend on the negotiation and no long form report is required, it is more important to establish a sound appreciation of the strengths and weaknesses of our negotiating position. A merchant bank is best placed to do this for us. And in any case Barings team includes people with accountancy qualifications.

8. It is not yet clear when the sale will take place, if indeed it can be negotiated. Given GEC's eagerness it is possible that it might take place before the end of the financial year.

*P C Diggle*

P C Diggle