

PO-CH/NL/0311

PART A

Part A.

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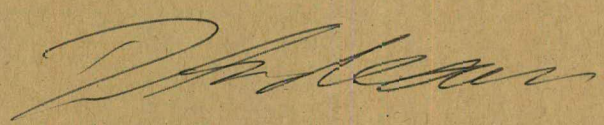

PO -CH /NL/0311

ART A

Chancellor's (Lawson) Papers :

THE FUTURE OF APPLIEDORE
AND FERGUSON
SHIPBUILDERS LIMITED

DD's : 25 Years



25/0/95.

PO -CH /NL/0311
PART A

25/1

dti

CONFIDENTIAL

the department for Enterprise

The Rt. Hon. Tony Newton OBE, MP
Chancellor of the Duchy of Lancaster and
Minister of Trade and Industry

Rt Hon John Major MP
Chief Secretary
HM Treasury
Parliament Street
LONDON
SW1P 3AG

CHIEF SECRETARY	
REC.	25 JAN 1989
ACTION	Mr Guy
COPIES TO	CX, FST, Sir P Middleton Mr Anson, Mr March, Mr Bugner Mr Mare, Mr BM White, Mr Best, Mr Rutnam, Mr Call.

Department of
Trade and Industry

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Our ref

Your ref

Date: 25 January 1989

Dear Chief Secretary,

APPLEDORE FERGUSON SHIPBUILDERS LIMITED: DEVON YARD

Thank you for your letter of 2 November in which you said you would be content for negotiations for the disposal of the Appledore yard to Langham Industries to move to a final position subject to a negative consideration of £1.7m, or less if possible, a charge on the site, and your officials being shown a Price Waterhouse assurance on minimum closure costs.

British Shipbuilders have now agreed terms on the basis of which they would be prepared to sell the yard to Langhams. With our agreement, they would hope to complete on Thursday 26 January. I am sorry not to have written to you sooner about this but it is only in the last day or so that the final details have been settled.

While the terms are not quite as advantageous as those looked for in your letter, I regard the proposed arrangements not only as a defensible but an acceptable basis on which to proceed. Clearance from the European Commission has already been obtained. The Corporation's Chairman and our respective financial advisers regard disposal as in the Corporation's commercial interest.

JA4ABG

⁹¹
The principle terms of disposal now agreed include a positive consideration of £1.6m consisting of £500,000 for the shares and £1.1m to reflect the expected state of the balance sheet on completion. Against this, BS would reimburse Langhams £1.15m for under-recoveries, £1.3m for redundancies and £1.3m for terms and conditions bought out from the workforce, mainly redundancy entitlements for the remaining 400 or so employees out of a present complement of 500.

The negative consideration of £1.7m to which you referred in your letter consisted of £500,000 for the shares net of estimated sums of £1m for redundancies and £1.2m for bought out terms. In practice Langham needed £1.3m to secure the deal they wanted with the workforce. The major change, increased cost of redundancies, reflects the actual entitlement of those who would go, and is higher than the earlier estimate based on the BS average because of the actual age and length of service of the employees affected. Neither figure is of direct benefit to Langhams and we would face the cost of redundancies in any event.

My officials have shown yours the material they received from Price Waterhouse. I accept the advice that closure on the basis forecast would be in the range of £7.5-£8.5m, aside from losses on BS obligations which would be incurred anyway. The PW team which provided the figures consulted their liquidators.

There is one change affecting the costs of closure and of disposal that has only recently come to light. BS always expected to have to concede the costs of losses on the existing workload in the yard. This workload consists of one of the Danish Ferries and two dredgers for ARC Marine and United Marine Aggregates respectively which our colleagues agreed on 19 November 1987 could be placed with Appledore in order to secure the eventual disposal of what at the time seemed to be the only BS facility likely to survive. What has now emerged is that the Corporation's commercial people, unaware of the wider issues we were discussing with colleagues, conceded an option to United Marine Aggregates to buy a further dredger on the same terms and conditions of the order we had agreed. UMA have pressed to exercise this option but have agreed the order could be placed with Langham to meet our preferences. Langham in turn have agreed with BS to take the order on completion subject to an offer from the Intervention Fund which I am inclined to make, indeed they have made the order a condition of their bid. They are insisting on a guarantee that BS would make good any losses attributable to their having mis-costed the vessel. Any other losses would fall to Langhams.

BS estimate that their exposure on this order should not be more than £400,000 and expect a lesser figure depending on the progress Langham make in reducing costs in the yard. In granting the option to UMA, BS were not in a position to commit my Department to a grant of Intervention Fund support though their client had no reason to expect it would be withheld against a background of previous orders at the yard. Were the sale of Appledore to be frustrated and we declined to support the Corporation in taking the order, BS expect UMA would seek legal redress given it would be impossible for them to secure a suitable alternative without much delayed delivery. I recognise this is an unfortunate development but the risk of damages strengthens the balance of costs argument in favour of disposal.

On the point about a charge on the property, BS have pursued with Langhams both a charge and a lease, which their lawyers regard as the most secure way of achieving a claim over any up-lift in value on disposal by Langhams. John Langham has rejected a lease since his bankers insist on a first charge on freehold property to secure necessary facilities for the business. He has also rejected a charge since he wants complete freedom to be able to use any increase in the value of his assets as security for further finance and bonding. Lazards for BS pressed again on this ground yesterday and have now advised BS in writing that to pursue the point further would only risk Langham's walking away. The delay in reaching a conclusion in this negotiation has been because the terms are finely balanced from Langhams' perspective given the risks they face in making a success of the business. Langhams have, however, been prepared to provide a letter of comfort, though I recognise that this falls short of a charge as you proposed.

I understand the reasons for a charge but there are no circumstances in this disposal which parallel those in which rationalisation might release land for substantial gain. Appledore is a compact operation on a single site with little land to spare. Moreover, Langhams seem committed to shipbuilding and if they failed, their losses seem bound to exceed the value of the assets in the yard by a substantial margin. Even a planned exit from shipbuilding would be costly given redundancy and other obligations. Also we know the Local Council is interested in retaining shipbuilding on the site, since they pressed for covenants to this effect, and may therefore be unwilling to give planning permission should it ever be sought for another purpose. This also argues against potential embarrassment on property for us.

JA4ABG

In all these circumstances I am prepared to endorse John Lister's recommendation that BS should now dispose of the Appledore yard to Langham. I should be grateful for your agreement. Following the closure of North East Shipbuilders and considerable uncertainties that have emerged about the disposal of Ferguson, I should be extremely reluctant to see the disposal of Appledore to Langham fail at this stage. I think we should find it far more difficult to defend a decision to frustrate this deal than any gain Langham might conceivably make as a result of it.

My apologies again for not having given you more notice of this.

Yours sincerely
Rosalind COTTE

pp TONY NEWTON

(approved by the Chancellor and signed
in his absence)

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FROM: W GUY
25 January 1989

CHIEF SECRETARY

cc Chancellor
Financial Secretary
Sir P Middleton
Mr Anson
Mr Monck
Mr Moore
Mr Burgner
Mr Bent
Mr Revolta
Mr AM White
Mr W White
Mr Tyrie
Mr Call

BRITISH SHIPBUILDERS: PRIVATISATION OF APPLIEDORE YARD

Mr Newton wrote to you this ^{afternoon} ~~morning~~ and now requires urgent agreement to the disposal terms for the Appledore yard so that the deal can be completed tomorrow or Friday. The handling of this by DTI has been a shambles. You are informed by Mr Newton that in effect all of the numbers for the deal which you saw earlier have changed; that he is not able to meet the clear conditions for disposal which you set in your letter of 2 November; and that the deal which he is now recommending involves an unquantified liability on British Shipbuilders and thence the Exchequer. He does not put it that way, but those are the facts. This last minute bounce is typical.

2. As in previous cases, the essential decision for you is whether to risk abortion of the disposal with its political consequences, or sign up immediately to a deal which, although the numbers involved are small, has a rather bad smell to it. The following sections explain the doubts about the proposed disposal terms and the way that they have been sprung on us. I am afraid that it is a typical tangle with no clearly preferable solution. *Mr. Newton clearly sees it as highly political.*

Background

3. You will recall that one subsidiary of BS is Appledore-Ferguson which has a yard (Ferguson) at Port Glasgow on the Clyde and one at Appledore in Devon employing about 500 people in the constituency of Mrs Emma Nicholson. It specialises in building dredgers and is currently working on two of them, one for a firm called UMA under a contract let in November 1987 just before colleagues agreed that BS should take no more orders. It is also building a ferry on subcontract from the Danish order at NEEL. Although regarded as the best run BS yard it is predictably losing money on all

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these orders, over and above the Intervention Fund costs, and is also scoring underrecoveries (costs which are not allocated to contracts when calculating contract losses).

4. The preferred bidder is Langham Industries, a small outfit without strong financial resources - it was reckoned unacceptable as a bidder for the Ferguson yard, which is a bigger cash drain, because it would be overstretched financially. In your letter of 2 November you set clear conditions for this disposal:-

(i) the negative consideration on disposal should be no more than £1.7m;

(ii) there should be a charge on the value of the site to prevent Langhams from shutting it as a shipyard and cashing a development gain for alternative use; and

(iii) we should have a stronger assurance from Price Waterhouse about the costs of closing the yard, which could be avoided by disposal.

5. This followed a correspondence in which you had successfully challenged Mr Newton's original assurance that disposal was far better than closure financially, and got him to revise his costings. We have since had further information from PW and we are content on this last point, albeit our view that closure costs are in fine balance with disposal costs remains.

The Land Charge

6. Since then we have heard from DTI officials that to place a charge on the alternative use land value would be legally impossible. We queried this and pointed out that it had been done successfully in a number of NBC disposals and was being done by BR for BREL. We asked to see their legal advice. Silence followed until earlier this week we were invited to sign up to the disposal terms at official level. I said that Mr Newton must write to you if he is not proposing to satisfy conditions (i) and (ii). Yesterday we got copies of the legal advice about a land charge which showed that it was difficult rather than impossible, and that the real point was that Langhams were insisting on having the full benefit of any alternative use premium for themselves.

7. On my insistence DTI officials returned to BS with the following argument: if Langhams envisage closing the yard and cashing in the land in the next few years, they must accept that BS is entitled to a share in any development gain. Valuations done for BS at our request show that Langhams could make a profit of about £1 million after all closure costs by doing this, subject to planning permission for medium density housing. If on the other hand Langhams can see nothing ahead but continued shipbuilding in a yard with no

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surplus land, a charge lasting for a few years would not hurt them. BS then met Langhams again and I heard from DTI this morning that the point was not negotiable, that Langhams had been very put out by it, and that they were threatening to walk away unless the deal was completed very soon now (tomorrow was given as the deadline), ~~but this has slipped for reasons below).~~

8. In discussion with DTI I stressed that this was a matter for your judgement, but that I would be prepared to advise you that the land should be seen as an endowment to Langhams in the interests of trying to preserve shipbuilding in the area. That is still my advice, assuming that you do wish to preserve shipbuilding there, with its associated economic costs. We are advised by BS, by their advisers Lazards, by DTI and by their advisers BZW that the only prospect for preserving the local shipbuilding industry is to sell to Langhams; and that Langhams are acting in good faith with a view to continued shipbuilding rather than asset stripping. They may need to mortgage the land to the hilt to raise working capital on top of the cash injections involved in our negative proceeds. Moreover the local authority has given evidence of opposition to anything other than industrial use of the land.

9. This would not have been a very ^{too much} satisfactory deal, but I could have recommended it without difficulty. However this morning I received a personal copy of the draft letter given to Mr Newton to send to you, which did not reach your office finally until 4pm today, from which we learned for the first time that there is another twist to the proposed deal involving a new order to build another dredger for UMA.

The New Order

10. We now know that in November 1987 when the UMA contract was accepted, BS gave UMA an option to place a further order with them on the same terms. UMA have recently notified that they are exercising this option. Since BS are forecasting a contract loss (in addition to IF) of £420,000 on the first UMA dredger (for the simple reason that they have found it costs £420,000 more to build one of these things than they thought when they fixed the price) it is a fair bet that they will make a loss honouring the option for a further order as well. Nobody outside BS knew about this until it cropped up recently in negotiation with Langhams. BS did not consider that the contingent liability to accept a further loss-making order was worth mentioning when earlier discussions about the yard were taking place. DTI did not tell us about it until this morning. But it has now become inextricably linked with the Langham bid, which turns out to be contingent on them accepting the order instead of BS, but with BS liable for any loss they might make in meeting it.

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11. This is startling. It is distinct from the arrangements which BS is making to honour existing contracts by subcontracting work to new owners, as in the case of the Chinese ships at Govan, the engines at Clark Kincaid and the existing workload at Appledore. It would not involve a fixed subcontract price to limit exposure. Instead, completion of the sale of Appledore to Langhams would take place simultaneously with and contingent upon the acceptance of the UMA contract by Langhams; and the sale terms would include a contractual obligation from BS to Langhams to make good the losses incurred by Langhams in meeting their contractual obligations to UMA. Mr Newton says this could cost £400,000. The key point is that it is open-ended.

12. Later this morning I impressed upon DTI that I could not recommend you to sign a blank cheque, and was surprised that Mr Newton should ask you to. I urged that a way be found to cap the exposure on the new order, for instance by having BS accept the order and subcontract it at a fixed price, or by limiting the obligation to Langhams. This, I am told, is now impossible without starting negotiations afresh and risking Langhams losing patience.

13. DTI have offered the following reassurances after further discussion with BS. First, BS will have an experienced man responsible for overseeing the contract with full access to Langhams papers and facilities. If he thinks Langhams are incurring costs unnecessarily, he will be able to warn them and subsequently BS will be able to litigate against any attempt to recover unnecessary or improperly charged costs from them. Second, Langhams will want to squeeze costs in the yard as fast and as far as possible, and will have no incentive to play the fool on the UMA contract just because BS is liable for losses on it. Third, Langhams will be able to learn from the mistakes BS made on the first UMA dredger. Fourth, all the costs will be subject to audit. Fifth, if we did put on a cap on the BS liability, Langhams would insist on it being very high and in the nature of these things, when you put on a cap all the audit you like will not stop expenditure rising to meet it. Sixth, there is no other place in this country to which BS could subcontract the order if it took it.

14. This is all very un reassuring for the following reasons, of which DTI is aware. First, oversight by an experienced BS hand is no consolation when it is experienced BS hands who have created this guaranteed loss-maker in the first place, and Appledore is only being sold not because the Government has lost patience with the wealth destruction perpetrated by UK shipbuilding in general (IF money continues to pour from the taxpayer into private sector shipbuilders) but because the Government despairs of BS ever finding out how to build a ship without turning in a major contract loss on top of IF. We have to wonder whether, in a terminal run-down, BS is not going to be more casual about the costs incurred by Langhams than it has been about its own costs (about which it has been

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very casual indeed).

15. Langhams may indeed be keen on cost reduction, but insulating them from the costs of this contract is not likely to help. They may muck about on this contract as a costless (to them) experiment from which to learn. And if they do hit the rocks and decide to strip the assets and run with a profit, they are not likely to be very cost conscious about the way that they finish this contract. Moreover if audit is no use in limiting costs when there is a cap in place, so much the less use is it when there is no cap at all. The contract surely could be accepted by BS and subcontracted abroad (politics aside).

16. None of this makes any impression on DTI's fait accompli: sign up to the deal or risk having to close the yard. The upside is that Langhams behaviour is consistent with commitment to shipbuilding, and this could offer continued shipbuilding activity and employment in an area where it is politically very sensitive. The total costs are modest in absolute terms, and probably not adrift from costs of closure by more than a few £million even if BS do get taken for a ride on the new order.

17. The downside is that the deal could go very rotten, with Langhams shutting the yard with profuse apologies about cash flow etc, bluffing the local authority into planning permission for a marina or such like, pocketing the development gain and adding insult to injury by making a complete hash of their work during the run down and passing the bill to BS (who will pass it straight to us).

The Overall Deal

18. PW have estimated the closure cost at £7.5m to £8.5m, plus obligations which would also be faced if it were sold to Langhams, such as some redundancy costs and the loss on the new order. In quibbling we might edge this down a little. And we can argue that by subcontracting the new order abroad, BS would save some losses on it. Against this needs to be set the costs of disposal, including the cost of future IF. Mr Newton gives figures which are not directly comparable with the limit of £1.7m on negative proceeds which you set. His numbers add up to negative proceeds of £2.15m, plus an open-ended liability estimated not to exceed £0.4m in respect of the new order. But some of these costs would arise on closure as well and so the total of £2.55m+ is not comparable with the £1.7m limit. It is impossible to extract a comparable figure from the jumble in Mr Newton's letter, but given an estimate that future IF for the yard could be worth £6m and that closure could cost as little as £7.5m, there is only £1.5m to play with before closure becomes preferable on narrow financial grounds. It is safe to say that the case for disposal to Langhams remains finely balanced, with perhaps a couple of £m either way (ie closure could be more or less

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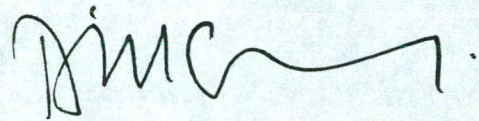
expensive than disposal by a couple of £m depending on the assumptions made).

18. This is not ideal. To agree to the deal would require faith in Langhams intentions and faith that DTI have got the numbers from which we are working more or less right, which given the history on this issue is not an easy assumption. But as it is DTI who are primarily in the firing line if the deal is bad, we ought to give some weight to their views. And we are in no position to pass judgement on Langhams intentions - we have never met them. We are struggling to follow developments at third hand and trying to influence the negotiations by remote control is very difficult (this is a further pragmatic reason for accepting the proposed deal: there is no telling what kind of mess could emerge from renegotiation if Langhams were prepared to reopen the deal).

19. You may wish to have a word with Mr Newton about this tomorrow morning - BS would still like to complete tomorrow if they can. You should be able to agree to his proposal if you shared his wish to do as much as possible to secure continued shipbuilding in the yard and if you were persuaded by him of the risk of the disposal aborting entirely if it were now renegotiated to limit the exposure from the new contract. Financially, the current proposal ^{may be} ~~is~~ probably worse than closure, but only by a few £million.

20. I regret that you are being pressed to take a complex decision with very little notice, but we and your office have repeatedly urged our opposite numbers in DTI to no avail to stop these bounces. We are in a weak position because it is not in our financial interests to abort things just to make a point about being tired of bounces, and any odium arising from the consequences of our insisting on taking time to think things over would be deflected to us as well.

21. I suggest that your response to Mr Newton is telephoned to his office tomorrow if you do not speak to him yourself, and we can then give you a draft letter to follow recording it.



W GUY

PM



FROM: P T WANLESS
DATE: 26 January 1989

MR GUY

Oh - Mr Guy's minute, behind, is splendidly splenetic.

PM B/C/S

has letter 6/10 PM

- cc:
- Chancellor
- Financial Secretary
- Sir Peter Middleton
- Mr Anson
- Mr Monck
- Mr Moore
- Mr Burgner
- Mr Bent
- Mr Revolta
- Mr A M White
- Mr Tyrie
- Mr Call

WZZ
CST
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CONV
CONV

BRITISH SHIPBUILDERS: PRIVATISATION OF APPLEDORE YARD

The Chief Secretary was extremely grateful for your excellent submission of 25 January which despite being prepared at such short notice provided him with clear and comprehensive advice.

2 The Chief Secretary is sure that Mr Newton is right about the politics of this case. In any event, within reason, he is inclined to support the prospect of saving jobs at Appledore rather than close a business because the disposal terms are marginally adverse.

3 However, the Chief Secretary feels strongly that the way DTI have handled this - as set out in your opening paragraph - is quite intolerable. Nor is this the first time, although he stresses that it must be the last. The Chief Secretary would be grateful for a draft letter to Mr Newton explaining bluntly that this cavalier treatment is both unreasonable and unsatisfactory. The Chief Secretary suggests that you might point out that he wrote to Mr Newton on 2 November, Mr Newton replied on 25 January seeking an answer on the same day although clearance from the EC had been obtained. Could

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we not have been informed at the same time? If not, why not? Moreover, why (paragraph 6 of your submission) did they advise us inaccurately and then not respond to our request to see the legal advice? And why did they not tell us of the contingent liability to provide a loss-making dredger? The Chief Secretary's view is that this surely is just plain incompetence.

PW

PETER WANLESS
Assistant Private Secretary

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FROM: W GUY

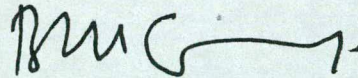
27 January 1989

CHIEF SECRETARY

cc Chancellor
FST
Mr Anson
Mr Monck
Mr Moore
Mr Bent
Mr W White
Mr Tyrie
Mr Call

BRITISH SHIPBUILDERS: APPLIEDORE

I attach a draft letter to Mr Newton which I hope has the balance right between something which the Department will be obliged to take seriously and something which would make Mr Newton feel that he has to try to mount a blustering defence of the indefensible, which though he could not sustain his case would generate an interminable correspondence. The draft details the history of relations with the DTI on this subject in case they are not all known to Mr Newton personally - although if he had looked back to your letters of 11 October and 2 November he ought to have realised that there was something seriously wrong with the Department's handling.



W GUY

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DRAFT LETTER TO MR NEWTON

BRITISH SHIPBUILDERS: DISPOSAL OF APPLEDORE FERGUSON DEVON YARD

Your letter of 25 January sought my agreement to the terms of disposal of the Appledore yard. The letter reached my office late that afternoon and I was asked to respond in time for the deal to be completed at a meeting which British Shipbuilders had arranged for the following morning. In the event I was able to do so and you will have heard of my agreement early on 26 January.

I have to make clear, however, that in agreeing to your proposal I was not indicating that I thought the terms offered were those which we should have got, nor even that I thought they were passably good. There were two aspects in particular which I found worrying. It was simply that I had apparently been placed in a position where if I did not promptly agree to the proposal exactly as you described it, there was a serious risk of the disposal aborting entirely with the loss of the Appledore business and its jobs. It was not necessary or reasonable to place me in that position, but you will recall that it was not the first time that it has happened and I specifically asked you last October not to let it happen again in this case.

I tried to help you to avoid it by opening a correspondence with you last Autumn about the terms which we should find acceptable. I was worried by the discrepancy between my officials' view that the full costs of disposal could be very close to the costs of closure requiring great care in setting disposal terms, and your Department's view that there was a wide margin in favour of disposal on financial grounds. I asked in my letter of 2 November that the negative consideration on disposal should be limited to £1.7m within the format of the table of numbers which was exchanged in my letter of 11 October and your reply of 31 October.

Since then your officials warned mine in general terms that the numbers were shifting because extra costs related to redundancy, common to both disposal and closure options, had been discovered. This of course does not affect the principle of comparing the avoidable costs of closure with the avoidable costs of disposal. That essential comparison is missing from your letter of 25 January, but it seems to me from the numbers which you do give that, even taking your own estimate of £6m for the present value of future IF to the yard, the costs of closure are indeed finely balanced with the costs of disposal, if not marginally outweighed by them, as I warned.

In my letter of 2 November I asked that a charge be placed on the alternative use value of the land involved in the

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disposal. The case for this is clear from information obtained subsequently by your Department which suggests that subject to planning permission the new owner could close the yard, satisfy all the costs associated with making the entire workforce redundant, and take a significant profit. I do not think it good to rely solely on a letter of comfort from the buyer which your officials admit to be legally unenforceable; and the desire of the local authority to preserve shipbuilding in the area does not mean that, faced with its termination, they would not sanction alternative use of the land to make the best of a bad job.

My officials were told that to place a charge on the alternative use premium as I asked would be impossible. Their request to see the relevant legal advice was not met until 24 January. That advice will be studied here for its implications for other privatisations, but its point seems to be not that my request was impossible but that it was being resisted by the buyer. But by this time negotiations had effectively concluded and we were told that to reopen them to meet my request would probably lead to abortion of the disposal.

The second aspect of the deal which I find particularly worrying is the open-ended liability to meet costs incurred by the buyer in fulfilling a contract to be placed with them to build a dredger for UMA. Although the existence of the option for this contract and its place in the negotiations had been known to your Department for some time, my officials were not told about it until the morning of 25 January. I regard the way in which it has been treated in the disposal negotiations as thoroughly unsatisfactory. But when my officials immediately reacted to news of it by urging that a way be found to limit BS' liability for the buyer's costs, they were told that it was inextricable from the overall disposal package and that, again, to attempt to renegotiate its treatment onto a more sensible basis would carry a strong risk of aborting the disposal.

The proposition with which you faced me on the evening of 25 January was therefore either to accept immediately the disposal terms which you described, with defects which I regard as unnecessary and peculiar features of which I had been kept ignorant until the last minute, or else to allow the whole disposal to founder.

I note that the European Commission has given clearance to the terms of the disposal. Since they would no doubt regard the arrangement concerning the new UMA order (involving as it does an unlimited guarantee to support their costs, which would otherwise fall on BS, in excess of IF limits) as being as odd from their perspective of regulating state aids as it is from mine of basic financial prudence, I would regard their clearance as unsafe unless they were aware of it. If they are aware of it I presume that they were told about it some time ago and that they were given more than a matter of

with the buyer

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hours in which to consider it.

In my letter of 11 October I asked that I should in due course have the opportunity to consider the options for Appledore with you without the sort of timing pressure to which I had been subjected in the disposals of Govan and Clark Kincaid. In the event it would not have been possible for you to consult me about this disposal any later than you did.

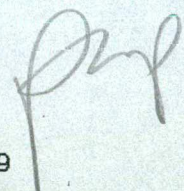
There are still difficult decisions ahead of us concerning the future of BS, such as the Ferguson yard. If I am to give your views on this and any other cases which arise the attention which they deserve and if you are to be in a position to respond constructively to my views I will need to hear from you at an earlier stage. I think that two clear working days should be the minimum which I am given, and that you do not allow negotiations to reach an irretrievable position before you have my views. I am sorry to have to write in these terms, but I am sure that you will agree that the handling of this case has been most unsatisfactory and must not be repeated.

JOHN MAJOR

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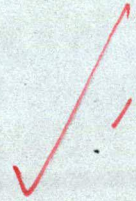
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FROM: W GUY
8 February 1989



CHIEF SECRETARY

cc Chancellor
FST
Mr Anson
Mr Monck
Mr Moore
Mr Burgner
Mr A M White
Mr Bent
Mr W White



BRITISH SHIPBUILDERS: FUTURE OF FERGUSON YARD

1. I have undertaken with DTI officials to consult you about the handling of imminent news that the disposal of the Ferguson yard has collapsed. They believe that Mr Newton will wish to reopen bidding for it, and that Mr Rifkind would object strongly if he did not. It would be helpful to take your view on this when we meet tonight to discuss rail links to the Channel Tunnel.
2. The Ferguson yard is at Port Glasgow on the Clyde. It has only one ship under construction - the second of the notorious ferries for Caledonian Mac Brayne (which is part of the nationalised Scottish Transport Group). That ship will be launched on 7 March by Mrs Rifkind. It is to be hoped that the ceremony will go rather better than that for the first of these two new CalMac ferries, which on settling in the water was noticed by those present to be rather low. Subsequent calculations revealed that it was so low in the water that if loaded with enough vehicles to make its operations economic, it would have been unsafe. Efforts to reduce weight by adapting the superstructure failed. The problem was traced to a fundamental fault in BS' designs for the hull. It had to be hauled out again, cut in half and have a new lightweight midsection inserted to ensure sufficient buoyancy. It was then found to be too long to fit CalMac's moorings. BS paid several million to have the moorings lengthened.
3. Assuming that the second vessel does not sink completely when Mrs Rifkind launches it, it will be fitted out by July after which the yard will have no more work at all. Redundancies could begin quite soon - there will be no more steelworking once the ship is in the water (accidents apart). There are currently **280** people employed at the yard. Although this is not a large number of jobs, and there is apparently a shortage of development land in that part of Clydeside, Mr Rifkind is known to feel strongly that no stone should be left unturned in efforts to preserve shipbuilding there.
4. Bids were invited for the yard last year, and a preferred bidder was selected. We have always thought it unlikely that a way could be found to dispose of Ferguson at a cost not

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exceeding the cost of closure, but the bidder was attempting to negotiate new working practices with the employees. The salient features of the package offered to the workforce were: a reduction in holidays from five weeks to four; sick pay reduced from generous BS levels to the statutory minimum; staff to be treated on the same terms as manuals; and no period of laying off on 75 per cent of pay before redundancy in the event that redundancies become necessary. It was thought that about 200 - 250 jobs could be preserved on this basis.

5. Yesterday the result of a ballot of the workforce showed 5 (five) in favour of this package, and 273 against. This scuppers the disposal. DTI officials advise that the workforce may not have regarded their action as suicidal, as they may believe that Mr Rifkind's support will ensure a better offer.

6. The bidder is meeting BS and DTI tomorrow to explore the scope for aid towards a large pay-off to buy out existing working practices. DTI officials believe that quite apart from the Treasury's attitude, the kind of sums which would be involved would seem too much to the European Commission. They regard this disposal as dead, and were minded to say so to the bidder tomorrow. As this would inevitably become public almost at once, they were going to advise Mr ~~Neckton~~ to answer an arranged question tomorrow confirming the termination of negotiations, but announcing that fresh bids for the yard would be accepted up to 31 March. They wanted to know if this invitation for new bids would be acceptable to the Treasury.

7. They present the merits of rebidding as follows:

(i) a new bidder may come forward;

(ii) a stay of execution would be consistent with the treatment of NESL;

(iii) it would avoid an argument with Mr Rifkind; and

(iv) it would save Mrs Rifkind from putting in an appearance before a crowd of shipworkers who had just all had notice of redundancy.

8. They point to Seaforth Defence International as a possible new bidder. They registered an interest after the original deadline for bids. They build small patrol and attack craft, which would not attract Intervention Fund support. But even so, there is only an outside chance of a satisfactory disposal to them, and in the meantime the redundancy programme would be delayed. DTI officials do not contest the view that rebidding would probably merely prolong the agony. They agree that a political defence of a prompt closure decision could be mounted. Bids were invited, negotiations ensued, and the fate of the yard has been sealed by the

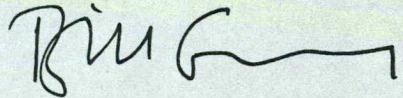
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refusal of the workforce to give up terms of employment which are wholly inappropriate to the current difficult shipbuilding market. But the Chairman of BS feels that it would look bad if Seaforth were not given a go, and Mr Newton is likely to want to show that he is exploring every avenue.

9. The financial arguments point to not allowing bidding to reopen, and that would put a clean end to the saga. But I said that as the problems were entirely political you would have to exercise your political judgement. Accordingly, BS and DTI will tomorrow refrain from telling the current bidder that the game with him is up, pending your views.

10. The issue for you is whether you are prepared to agree to new bids being accepted up to 31 March, or whether you wish to take on Mr Newton and Mr Rifkind and insist on an immediate decision to close. The money involved is not very great.

11. If you were minded to do Mr Rifkind a favour, you could say that the period for new bids should expire on, say, 15 March; that it should be made clear that it is the final chance; and that if a bidder comes forward a decision should be taken to close the yard and begin redundancies if negotiations have not demonstrably moved towards a satisfactory basis for disposal by, say, the end of April



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