

PO-CH/0329 PTA

Part. A.

Begins: 13/7/87.
Ends: 20/12/89.



PO -CH /NL/0329



PART A

Chancellors (Lawson) Papers:

MEETINGS WITH THE
NATIONALISED INDUSTRIES
CHAIRMENS GROUP

DD's: 25 Years

3/11/95.

PO -CH /NL/0329

PART A

2229/24

PPS/CHIEF SECRETARY

RF . Pps
DATE: 13 July 1987

cc PPS *such*

Mr F E R Butler
Mr Kemp
Mr Monck
Mr Moore
Mr Houston
Mr Colman (or)
Mr Gilhooly
Mr Williams
Mr Marr

NATIONALISED INDUSTRIES' CHAIRMEN'S GROUP

The Chancellor has asked the Chief Secretary to meet the NICG on Board pay, as requested in Sir Robert Reid's letter of 30 June. (Copies attached for copy recipients - I am not sure how widely it has been circulated).

2. You asked for advice on this. I think the Chief Secretary must agree to see the NICG reasonably soon - probably before the Recess unless there is any chink in the diary between the summer holidays and the build-up of work on the bilaterals. We expect considerable pressure on Board salaries from sponsor Ministers over the next few months, and the Chief Secretary may find it helpful to talk to the Chairmen at a fairly early stage. The NICG came to see his predecessor for a similar meeting in March 1986.

3. As the Chancellor's office has already responded to Sir Robert's letter, I suggest that you simply telephone the NICG and ask when they would like to come in. It would be desirable to keep the meeting fairly small, and Sir Robert has already indicated that this is what he has in mind. You should also ask for an indication of any specific points they wish to raise.

'4. We will brief for the meeting when it is arranged.

Mary Brown

MRS M E BROWN



FROM: JULIE LONG
DATE: 8 July 1987

PS/CHIEF SECRETARY

*c.c. Mr Moore
Mrs Brown*

NATIONALISED INDUSTRIES' CHAIRMEN'S GROUP

Attached is a copy of a letter the Chancellor has received from the Chairman of the Nationalised Industries' Chairmen's Group. The Chancellor has agreed to join the NICG for dinner (marked X in the margin), and has suggested that the Chief Secretary take on Y. I have written separately to the NICG asking them to get in touch with you.

Julie Long

JULIE LONG

Nationalised Industries' Chairmen's Group

Chairman
Sir Robert Reid, CBE,

Hobart House
Grosvenor Place
London SW1X 7AE

01-235 2020

30th June, 1987

The Rt. Hon. Nigel Lawson, M.P.,
Chancellor of the Exchequer,
Treasury Chambers,
Parliament Street,
London, SW1P 3AG.

Dear Nigel,

My colleagues and I would like to convey our congratulations to you on your re-appointment as Chancellor of the Exchequer. We wish you well in the tasks that lie ahead.

Although Privatisation is at the heart of the Government's policy towards the Corporations it is, as you know, an issue on which the Chairmen's Group has always refrained from taking up any position. At the level of principle, we have throughout regarded the prolonged debate about public or private ownership as an essentially political matter, for decision by the Government and Parliament. And at the practical level, responses to specific legislative proposals affecting particular industries are a matter which we leave to individual Chairmen, in the light of the circumstances of their own businesses.

At best, however, Privatisation will take an appreciable time to complete. Thus, there will also remain need, for some time to come, to consider how best those Corporations remaining in public ownership can maximise their contributions to the nation's economic well-being.

Responsibility in this regard rests, of course, primarily with the Corporations themselves. During the life of the last two Parliaments, the public sector businesses have passed through a difficult period of adjustment, but we have emerged much stronger in terms of our efficiency and we are much better placed in terms of our aggregate profitability. Looking ahead, my colleagues and I are determined to move still further ahead in those two directions over the next five years.

Cont'd.....

The Corporations' results are, however, considerably affected by Ministerial policies and practices, so we must look to the Government to help by following courses which reinforce our efforts to enhance the efficiency and profitability of our businesses. For the most part, any policy problems arising in this regard fall to be pursued by Chairmen on an individual basis with their own sponsor Secretaries of State. However, there are also a limited number of major issues of common concern which can only be pursued by way of collective discussion. The Chairman's Group therefore looks forward to a continuing productive dialogue with you, the sponsor Secretaries of State and the Chief Secretary on issues of that sort.

In that connection, I should like to suggest three early steps.

X Firstly, I trust that you will agree to reinstate sometime this Autumn the Ministerial-N.I.C.G. dinner-meeting which you originally blessed in your letter of 19th January, but which subsequent events conspired to frustrate. Subject to your agreement, I shall write to you in a week or two, after I have had a chance to consult my colleagues, to suggest some of the issues which we might then consider.

4. Secondly, I hope that you will also be able to find time for a further, smaller meeting in the reasonably near future to discuss Board salary matters, on which a very considerable head of steam has built up.

Thirdly, I shall shortly be writing to the Chief Secretary, requesting a meeting with him, mainly designed to bring to a head the long-drawn-out exchanges at official level on the Corporations' accounting practices.

In addition, I should like to leave in your mind that my colleagues and I found the dinner-meeting which we had with the Prime Minister in November 1985 an encouraging and stimulating occasion. We very much hope that it will be possible to repeat it, in one form or other, before too long.

I am copying this letter to the Prime Minister's office, to the sponsor Secretaries of State and to the Chief Secretary.

Tom Curran

BR

BOB REID

Nationalised Industries' Chairmen's Group

Chairman
Sir Robert Reid, CBE,

Hobart House
Grosvenor Place
London SW1X 7AE

23rd September, 1987

01-235 2020

The Rt. Hon. John Major, M.P.
Chief Secretary to the Treasury
Treasury Chambers,
Parliament Street,
London, SW1P 3AG.

CHIEF SECRETARY	
REC.	25 SEP 1987
	Mr Colman
10	EX PMG Mr Kenyon
	Mr Marsh
	Mr Moore Mrs Brown
	Mr Tyne.

Ree Chief Secretary

Accounting Practices

When I wrote to you on 14th August asking for a meeting to discuss Board salaries I mentioned that we should also like to discuss "the Corporations' accounting practices, in the context of the prolonged follow-up talks on the Report of a Treasury Advisory Group on 'Accounting for Economic Costs and Changing Prices'". Since the date when we are to meet has moved back to November, it may be convenient if I let you know our thinking on that issue ahead of the meeting.

Following receipt of the Treasury Advisory Group's Report, Philip Jones sent John MacGregor, on 16th May 1986, a memorandum setting out the Group's policy-level observations on the document, together with an appendix commenting on the technical accounting issues involved. We also questioned whether, in the light of the fact that Ministers had refrained from endorsing its recommendations, the Report provided a suitable basis for formal discussions between the Government and the Corporations. After correspondence, however, and at John MacGregor's specific request, we agreed to set aside for the time being both the policy-level criticisms which we had made of the Report and our reservations about its status, and to enter into follow-up talks limited to the technical accounting recommendations which it put forward.

Those technical follow-up talks have since gone on for the best part of a year, both on a Corporation-by-Corporation basis and on a collective basis. On our count there have been 21 such meetings; and they have not only ranged over all the main recommendations of the Report, but have necessarily considered in some depth some of the underlying accounting concepts. I think we can reasonably claim, therefore, to have fully complied with the promise which we made to your predecessor, and to have given the authors of the Report an exceptional opportunity to make the case for their recommendations.

Cont'd.....

All those involved on our side have found these talks stimulating; and I understand that some of those involved have been persuaded that some of the specific suggestions put forward in the Report have relevance in the context of their own Corporation's business situations, and are consonant with existing statements of accounting principles and with statutory requirements. On the other hand, preparing for and participating in these high-level seminars have absorbed a not-inconsiderable part of the time of our finance staffs over a period of nearly a year; and Chairmen naturally feel that there are other ways in which these people can make a more direct contribution to reducing our costs and increasing our profitability. Accordingly, when my colleagues and I met recently, we all agreed that the time had come to bring these prolonged follow-up talks on technical accounting issues to a close.

What now remains is to pull out from all these discussions whatever practical benefits we can. This not a matter for the Chairmen's Group as such, but for the individual Boards. Accordingly, my colleagues and I have agreed that each Corporation will now give serious consideration to the question of whether it has been sufficiently persuaded by what has passed during the follow-up talks to alter its accounting practices in any respects. Corporations will, of course, keep their sponsor Departments informed as events unfold.

If you are content to let matters move forward on this basis, we shall not need to take up your time discussing the "accounting practices" issue when we meet in November. However, if Ministers were of a mind to impose any of the Report's recommendations, irrespective of the views of the individual Board concerned, then we should, of course, wish to see the issue kept on the agenda for the meeting. Moreover, we should then want to take up your predecessor's promise that, before any question arose of taking decisions on the Report's recommendations, the Group would be given an opportunity to discuss fully the policy-level objections to the Treasury Advisory Group's proposals set out in our memorandum of 16th May 1986, which have so far been left on one side while the technical accounting aspects of the Report have been examined.

Tom Smith

Bob Reid
BOB REID

FROM: N MONCK

DATE: 12 October 1987

RS

CHIEF SECRETARY

cc PS/Chancellor
Paymaster General
Sir P Middleton
Mr F E R Butler
Mr A Wilson
Mr Byatt
Mr Moore
Mrs M Brown
Mr Colman
Mr Houston
Mr M Williams
Mr Inglis
Mr Tarkowski

NATIONALISED INDUSTRIES' CHAIRMEN'S GROUP AND THE BYATT REPORT

Sir Robert Reid, Chairman of British Rail, wrote to you on 23 September in his capacity as Chairman of the Nationalised Industries Chairmen's Group (NICG). The letter was a helpful one. It effectively withdrew, conditionally, the NICG's earlier request to discuss with you the Byatt Report on "Accounting for Economic Costs and Changing Prices" in the Nationalised Industries. (I set out the background in my minute to you of 16 July, along with our aim of rounding off the discussions of the Report with the industries and others by arranging a low key written PQ soon after Parliament returns.) This note recommends you to write to sponsor Ministers to clear the draft PQ which should fit in well with the NICG letter.

2. The first part of the letter is characteristic of the NICG bureaucrats, restating the NICG's earlier points of principle and making a lot of the length and number of the follow up talks and the industries' graciousness in agreeing to take part in them. In fact 21 meetings is not unreasonable since 12 separate industries were involved and Mr Byatt's central group met six times to deal with what is necessarily a complex and in parts innovative Report. The second page of the letter, however, acknowledges that the talks were stimulating and produced some agreement and desirable changes. It proposes that each Corporation should now consider whether and how it should alter its accounting practices in the light of the Report and the discussions. (Some of the industries are likely to make changes as a result of these exchanges.) No central discussion with you will be needed provided that Ministers do not intend to impose any of the Report's recommendations irrespective of the views of individual Boards.

3. Our advice is that you should accept this proviso which is indeed consistent with the thrust of the draft PQ attached, which we have now amended in the light of sponsor Departments' comments.

4. I attach a draft letter for you to send to Lord Young and other sponsoring Ministers, attaching both Sir Robert Reid's letter to you and the draft PQ.

5. Although the PQ has been cleared with their officials, we will have to give them a week or so to reply. I therefore suggest that your Private Secretary should write to Sir Robert Reid's saying that you were grateful for his letter of 23 September and that you hope to reply shortly.



N MONCK

DRAFT LETTER FOR THE CHIEF SECRETARY TO SEND LORD YOUNG

THE NATIONALISED INDUSTRIES AND THE REPORT ON "ACCOUNTING FOR ECONOMIC COSTS AND CHANGING PRICES"

A Report on "Accounting for Economic Costs and Changing Prices" was commissioned by the Treasury in 1984 and was published last August. The Report was prepared by a group of outside accounting experts, chaired by Mr Byatt, the Treasury's Deputy Chief Economic Adviser. When the Government published the Report, it said that sponsor Departments and the Treasury would discuss the general principles in it, their merits and their practical application with individual nationalised industries, the Nationalised Industries Chairmen's Group and other interested parties. The NICG agreed to the discussions taking place at a technical level.

2. The follow up discussions are now complete and it has been agreed at official level that they should be rounded off with a low key written Parliamentary Question. I attach a draft of this which has been amended in the light of your officials' comments.

3. I also attach a copy of a letter which Bob Reid has sent me. The letter is helpful. It acknowledges that the discussions have been useful and proposes that each Corporation should consider whether and how it should alter its accounting practices in the light of the Report and the discussions. This fits in well with the thrust of the draft Parliamentary Answer.

4. Subject to any comments by [20] October, I propose to write to Bob Reid, thanking him for his helpful letter and saying that it fits in well with the enclosed draft Parliamentary Answer which I propose should round off these discussions.

5. I am sending copies of this letter and attachments to Nicholas Ridley, Cecil Parkinson, Paul Channon and Peter Walker.

[J.M.]

DRAFT PQ AND ANSWER

Q. To ask Mr Chancellor of the Exchequer if he will make a statement on the accounting policies of nationalised industries in the light of the discussions which have taken place on the report, Accounting for Economic Costs and Changing Prices, published in August 1986.

A. Successive governments have pointed out the desirability of making due allowance for changing prices in company accounts. This is particularly important in businesses where, as in many of the nationalised industries, assets are long lived and where rates of return based on historic cost are inadequate as measures of economic performance.

2. The nationalised industries have been at the forefront of the development of current cost accounting. The Government has welcomed this and notes that some of the industries which have been privatised, in particular those subject to regulation, have decided to maintain current cost accounts. It has noted that the Director General of Telecommunications has proposed that British Telecommunications should publish information on current cost profits.

3. When the Government published the report of the Advisory Group, Accounting for Economic Costs and Changing Prices, it said that sponsor departments and the Treasury would discuss the general principles described in the report, their merits and their practical application with individual nationalised industries, the Nationalised Industries' Chairmen's Group and other interested parties. Discussions with the individual industries and with the Chairmen's Group have now taken place. There have also been comments by the accountancy bodies and wider discussions.

4. These discussions, which have been at a technical level throughout, have revealed broad agreement among the majority of industries on the principles on which economic costs should be measured. They have indicated ways in which some of the recommendations in the report should be modified, but have also indicated ways in which practice might be usefully developed. They have identified certain problems which require further study. They have shown the conditions under which modified historical cost accounts can be used to measure economic performance. These are that in those

accounts the revaluations should cover all assets and be regularly up-dated, and that revalued assets are consistently treated in both the profit and loss account and balance sheet. The discussions have underlined the importance of the distinction made in the report between industries with a substantial degree of influence over their prices - the "price-makers"; and industries whose prices are determined in competitive markets - the "price-takers".

5. The Government is satisfied with the outcome of the discussions and does not propose to take any immediate action. The discussions have been useful in confirming that the present accounting policies of nationalised industries go a long way towards the objective of providing measures of economic costs and that some further progress is in prospect. Present accounting policies should be maintained and reviewed in a year or two so that they continue to develop in ways which fulfil this objective. The report can provide a framework for judging such evolution.

27/13a

Nationalised Industries' Chairmen's Group

Chairman
Sir Robert Reid, CBE,

Hobart House
Grosvenor Place
London SW1X 7AE

23rd September, 1987

01-235 2020

The Rt. Hon. John Major, M.P.
Chief Secretary to the Treasury
Treasury Chambers,
Parliament Street,
London, SW1P 3AG.

CHIEF SECRETARY	
REC.	25 SEP 1987
FILE	Mr Colman
10	CX PMG Mr Kenyon
	Mr Mendel
	Mr Moore Mrs Brown
	Mr Tyne.

Dear Chief Secretary

Accounting Practices

When I wrote to you on 14th August asking for a meeting to discuss Board salaries I mentioned that we should also like to discuss "the Corporations' accounting practices, in the context of the prolonged follow-up talks on the Report of a Treasury Advisory Group on 'Accounting for Economic Costs and Changing Prices'". Since the date when we are to meet has moved back to November, it may be convenient if I let you know our thinking on that issue ahead of the meeting.

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Cont'd.....

All those involved on our side have found these talks stimulating; and I understand that some of those involved have been persuaded that some of the specific suggestions put forward in the Report have relevance in the context of their own Corporation's business situations, and are consonant with existing statements of accounting principles and with statutory requirements. On the other hand, preparing for and participating in these high-level seminars have absorbed a not-inconsiderable part of the time of our finance staffs over a period of nearly a year; and Chairmen naturally feel that there are other ways in which these people can make a more direct contribution to reducing our costs and increasing our profitability. Accordingly, when my colleagues and I met recently, we all agreed that the time had come to bring these prolonged follow-up talks on technical accounting issues to a close.

What now remains is to pull out from all these discussions whatever practical benefits we can. This not a matter for the Chairmen's Group as such, but for the individual Boards. Accordingly, my colleagues and I have agreed that each Corporation will now give serious consideration to the question of whether it has been sufficiently persuaded by what has passed during the follow-up talks to alter its accounting practices in any respects. Corporations will, of course, keep their sponsor Departments informed as events unfold.

If you are content to let matters move forward on this basis, we shall not need to take up your time discussing the "accounting practices" issue when we meet in November. However, if Ministers were of a mind to impose any of the Report's recommendations, irrespective of the views of the individual Board concerned, then we should, of course, wish to see the issue kept on the agenda for the meeting. Moreover, we should then want to take up your predecessor's promise that, before any question arose of taking decisions on the Report's recommendations, the Group would be given an opportunity to discuss fully the policy-level objections to the Treasury Advisory Group's proposals set out in our memorandum of 16th May 1986, which have so far been left on one side while the technical accounting aspects of the Report have been examined.

Tom Smith

Bob Reid
BOB REID



Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Lord Young of Graffham
 Secretary of State for Trade and Industry
 Department of Trade and Industry
 1 - 19 Victoria Street
 London
 SW1H 0ET

CC-CX, AMG

2

Mr. P. Middleton, Mr. Butler

Mr. Brown, Mr. A. Wilson

Mr. Byatt, Mr. Hoare

Mr. Brown, Mr. Colman

Mr. Houston, Mr. M. Williams

Mr. Jarvis

Mr. Tarkenton

ND

19 October 1987

Dear David,

**THE NATIONALISED INDUSTRIES AND THE REPORT ON
 "ACCOUNTING FOR ECONOMIC COSTS AND CHANGING PRICES"**

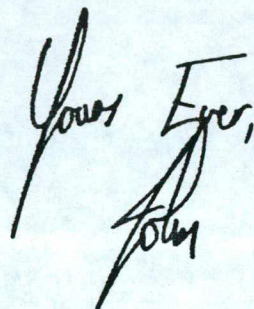
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The follow up discussions are now complete and it has been agreed at official level that they should be rounded off with a low key written Parliamentary Question. I attach a draft of this which has been amended in the light of your officials' comments.

I also attach a copy of a letter which Bob Reid has sent me. The letter is helpful. It acknowledges that the discussions have been useful and proposes that each Corporation should consider whether and how it should alter its accounting practices in the light of the Report and the discussions. This fits in well with the thrust of the draft Parliamentary Answer.

Subject to any comments by 23 October, I propose to write to Bob Reid, thanking him for his helpful letter and saying that it fits in well with the enclosed draft Parliamentary Answer which I propose should round off these discussions.

I am sending copies of this letter and attachments to Nicholas Ridley, Cecil Parkinson, Paul Channon and Peter Walker.

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

JOHN MAJOR



SECRETARY OF STATE FOR ENERGY

THAMES HOUSE SOUTH
MILLBANK LONDON SW1P 4QJ

01 211 6402

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

CHIEF SECRETARY
28 OCT 1987
<i>Mr Monck</i>
<i>CX PMS Sir Peter Middle</i>
<i>Mr Butler Mr Adlam</i>
<i>Mr Byatt Mr Moore</i>
<i>Mr Brown Mr Colman</i>

28 October 1987

Mr Houston Mr M Williams
Mr Inglis Mr Taskowski

Dear John

THE NATIONALISED INDUSTRIES AND THE REPORT ON
"ACCOUNTING FOR ECONOMIC CUTS AND CHANGING PRICES"

Thank you for your letter of 19 October. It appears that some good work has been done in the discussions with the industries. I am content with the draft Parliamentary answer which you circulated.

Yours
Cecil
Parkinson

CECIL PARKINSON

CC - CX, AMG, Sir P Mordaunt

2 Mr Botter, Mr A Wilson

Mr Byatt, Mr Moore

Mr Brown, Mr Colman

Mr Haslam, Mr M Williams

Treasury Chambers, Parliament Street, SW1P 3AG Mr Inglis

Mr Tinkler



Sir Robert Reid CBE
Nationalised Industries' Chairmen's Group
Hobart House
Grosvenor Place
London
SW1X 7AE

ND

30 October 1987

Dear Sir Robert,

ACCOUNTING PRACTICES: BYATT REPORT

Thank you for your helpful letter of 23 September on this subject. I was glad to hear that both sides found the follow-up discussions useful.

We agree with you that now the talks are completed, the next step should be for each corporation to consider whether and how it should alter its accounting practices in the light of the Report and the discussions. I think it would be right to round off the discussions with a written Parliamentary Answer. I propose to ... answer an arranged question along the lines of the attached text which I have agreed with my colleagues. I hope you will agree that it fits in well with the thrust of your letter to me (which I circulated to sponsor Ministers). If we can go ahead on this basis, I agree that there would be no need for us to discuss accounting when we meet next month.

It was kind of you to call + see me this morning + I much enjoyed our chat. I look forward to our further discussion in a few days trip with your colleagues.

Yours Sincerely,
John Major

JOHN MAJOR

DRAFT PQ AND ANSWER

Q. To ask Mr Chancellor of the Exchequer if he will make a statement on the accounting policies of nationalised industries in the light of the discussions which have taken place on the report, Accounting for Economic Costs and Changing Prices, published in August 1986.

A. Successive governments have pointed out the desirability of making due allowance for changing prices in company accounts. This is particularly important in businesses where, as in many of the nationalised industries, assets are long lived and where rates of return based on historic cost are inadequate as measures of economic performance.

2. The nationalised industries have been at the forefront of the development of current cost accounting. The Government has welcomed this and notes that some of the industries which have been privatised, in particular those subject to regulation, have decided to maintain current cost accounts. It has noted that the Director General of Telecommunications has proposed that British Telecommunications should publish information on current cost profits.

3. When the Government published the report of the Advisory Group, Accounting for Economic Costs and Changing Prices, it said that sponsor departments and the Treasury would discuss the general principles described in the report, their merits and their practical application with individual nationalised industries, the Nationalised Industries' Chairmen's Group and other interested parties. Discussions with the individual industries and with the Chairmen's Group have now taken place. There have also been comments by the accountancy bodies and wider discussions.

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5. The Government is satisfied with the outcome of the discussions and does not propose to take any immediate action. The discussions have been useful in confirming that the present accounting policies of nationalised industries go a long way towards the objective of providing measures of economic costs and that some further progress is in prospect. Present accounting policies should be maintained and reviewed in a year or two so that they continue to develop in ways which fulfil this objective. The report can provide a framework for judging such evolution.



DEPARTMENT OF TRADE AND INDUSTRY

1-19 VICTORIA STREET
LONDON SW1H 0ET

Telephone (Direct dialling) 01-215) 5147
GTN 215) 5147
(Switchboard) 01-215 7877

From the Chancellor of the Duchy of Lancaster
and Minister of Trade and Industry

THE RT HON KENNETH CLARKE QC MP

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

CHIEF SECRETARY the Treasury	
REC.	28 OCT 1987
ACTED	Mr Monck
TO	CX PMG Sir Peter Middleton
	Mr Butler Mr A Wilson
	Mr Byatt Mr Moore
	Mrs Brown Mr Colma

28 October 1987

Dear John,

Mr Houston Mr M Williams
Mr Inglis Mr Taskowski

THE NATIONALISED INDUSTRIES AND THE REPORT ON "ACCOUNTING FOR
ECONOMIC COSTS AND CHANGING PRICES"

Thank you for your letter of 19 October to David Young about the conclusion of the discussions with the Nationalised Industries' Chairman's Group and the individual industries on the Byatt Report and its applicability to the industries.

Although the circumstances of the industries for which my Department is responsible vary widely, the round of discussions has been useful in improving understanding even if views remain widely different in some cases about the practicability or even desirability of espousing the principles enunciated in the Byatt Report. I agree that we should see how the industries' accounting policies develop in the light of the discussions and review the position in a year or two's time.

I am content with the terms of the proposed Parliamentary Answer and that you should reply to Bob Reid on the lines suggested.

I am copying this letter to Nicholas Ridley, Cecil Parkinson, Paul Channon and Peter Walker.

KENNETH CLARKE

FROM: N MONCK

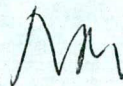
DATE: 28 October 1987

CHIEF SECRETARY

cc PS/Chancellor
Paymaster General
Sir P Middleton
Mr F E R Butler
Mr A Wilson
Mr Byatt
Mr Moore
Mrs M Brown
Mr Colman
Mr Houston
Mr M Williams
Mr Inglis
Mr Tarkowski

NATIONALISED INDUSTRIES' CHAIRMEN'S GROUP AND THE BYATT REPORT

None of the nationalised industries sponsor Ministers have objected to your letter of 19 October or to the attached draft Parliamentary answer, designed to round off the follow-up discussions about the Byatt Report. The way is therefore clear for you to write to Sir Robert Reid, as Chairman of the Nationalised Industries Chairmen's Group. I attach a draft letter, covering the draft PQ.



N MONCK

DRAFT LETTER FOR THE CHIEF SECRETARY TO SEND TO SIR ROBERT REID

ACCOUNTING PRACTICES : BYATT REPORT

Thank you for your helpful letter of 23 September on this subject. I was glad to hear that both sides found the follow-up discussions useful.

2. We agree with you that now the talks are completed, the next step should be for each corporation to consider whether and how it should alter its accounting practices in the light of the Report and the discussions. I think it would be right to round off the discussions with a written Parliamentary Answer. I propose to answer an arranged question along the lines of the attached text which I have agreed with my colleagues. I hope you will agree that it fits in well with the thrust of your letter to me (which I circulated to sponsor Ministers). If we can go ahead on this basis, I agree that there would be no need for us to discuss accounting when we meet next month.

[JM]

DRAFT PQ AND ANSWER

- Q. To ask Mr Chancellor of the Exchequer if he will make a statement on the accounting policies of nationalised industries in the light of the discussions which have taken place on the report, Accounting for Economic Costs and Changing Prices, published in August 1986.
- A. Successive governments have pointed out the desirability of making due allowance for changing prices in company accounts. This is particularly important in businesses where, as in many of the nationalised industries, assets are long lived and where rates of return based on historic cost are inadequate as measures of economic performance.
2. The nationalised industries have been at the forefront of the development of current cost accounting. The Government has welcomed this and notes that some of the industries which have been privatised, in particular those subject to regulation, have decided to maintain current cost accounts. It has noted that the Director General of Telecommunications has proposed that British Telecommunications should publish information on current cost profits.
3. When the Government published the report of the Advisory Group, Accounting for Economic Costs and Changing Prices, it said that sponsor departments and the Treasury would discuss the general principles described in the report, their merits and their practical application with individual nationalised industries, the Nationalised Industries' Chairmen's Group and other interested parties. Discussions with the individual industries and with the Chairmen's Group have now taken place. There have also been comments by the accountancy bodies and wider discussions.
4. These discussions, which have been at a technical level throughout, have revealed broad agreement among the majority of industries on the principles on which economic costs should be measured. They have indicated ways in which some of the recommendations in the report should be modified, but have also indicated ways in which practice might be usefully developed. They have identified certain problems which require further study. They have shown the conditions under which modified historical cost accounts can be used to measure economic performance. These are that in those

accounts the revaluations should cover all assets and be regularly up-dated, and that revalued assets are consistently treated in both the profit and loss account and balance sheet. The discussions have underlined the importance of the distinction made in the report between industries with a substantial degree of influence over their prices - the "price-makers"; and industries whose prices are determined in competitive markets - the "price-takers".

5. The Government is satisfied with the outcome of the discussions and does not propose to take any immediate action. The discussions have been useful in confirming that the present accounting policies of nationalised industries go a long way towards the objective of providing measures of economic costs and that some further progress is in prospect. Present accounting policies should be maintained and reviewed in a year or two so that they continue to develop in ways which fulfil this objective. The report can provide a framework for judging such evolution.

Nationalised Industries' Chairmen's Group

Handwritten initials

Chairman
Sir Robert Reid, CBE,

Hobart House
Grosvenor Place
London SW1X 7AE

11th November, 1987

01-235 2020

The Rt. Hon. John Major, M.P.,
Chief Secretary to the Treasury,
Treasury Chambers,
Parliament Street,
London, SW1P 3AG.

CHIEF SECRETARY	
REC.	13 NOV 1987
MR MAURICE	
MR MAURICE, SIR PHILIP AGOSTON, MR BOTTLER	
MR AWILSON, MR BYATT, MR BOGEE	
MR BROWN, MR COLMAN, MR HASTON	
MR M WILKINSON, MR JAGUS,	
MR TAYLOR	

Handwritten number 2

Dear Chief Secretary

Accounting Practices : Byatt Report

Thank you for your letter of 30th October about the Corporations' accounting practices in the context of the Byatt Report.

I am very glad to see that we are at one in the view that it should ~~not~~^{not} be left to individual Corporations to decide whether they have been sufficiently persuaded by what they have heard to wish to change their accounting practices in any respects. I can assure you that my colleagues and I, and our Finance Directors, will take very seriously our commitment to undertake that review.

I am also happy to go along with your view that the outcome of the consultation ought to be explained publicly, by way of a Parliamentary Answer.

I hope, however, that you will allow us a little time to consider the text which you sent me before you move ahead in that connection. We have a natural interest in paras. 4 and 5 in particular, since these bear on the Corporations' reactions to the Report and what they may do next.

Like you, I now see no reason to discuss this accounting practice issue substantively when we meet next Thursday. Any exchanges about the drafting of your Parliamentary Answer can perhaps be left to our officials.

Handwritten signature

Handwritten signature

BOB REID

FROM: D J L MOORE
DATE: 18 NOVEMBER 1987

PS/CHANCELLOR

cc: PS/Chief Secretary
PS/Financial Secretary
Sir Peter Middleton
Mr Anson
Mr Monck
Mr Burgner
Mr Hawtin
Mr FK Jones
Mr Gilhooly
Mrs ME Brown
Mr Colman
Mr ML Williams
Mr Tarkowski
Mr Call

*Ch / Content for me
to write as proposed?*

OK - JH 18/11

**MINISTERIAL/NICG DINNER
ON WEDNESDAY 2 DECEMBER**

Mr Driscoll of the NICG has told me that the Chairmen would like to discuss 3 topics with Ministers at the dinner on 2 December. They are the relationship between Government and the nationalised industries that are likely to stay in the public sector for some time; the Community's plans for completing the internal market by 1992, with particular reference to public purchasing by the nationalised industries; and some ideas they are developing for their contribution to Inner City and training initiatives.

2. This seems acceptable and, if the Chancellor is content with it, I suggest you write to the Private Secretaries of the other Ministers concerned as in the attached draft letter which describes the agenda more fully.

3. We have no topics which we suggest Ministers should add to the agenda. In practice the first item, on the relationship, is a convenient catch-all. We will include in the briefing, for use as necessary, a note on pay. The Chairmen do not want a substantive discussion of Board pay and appointments which they covered at their meeting with the Chief Secretary last week.

4. We will put forward briefing next week. The usual drill on these occasions is for the Treasury briefing to be circulated to the other Ministers.

DJM

D J L MOORE

Enc:

DRAFT PRIVATE SECRETARY LETTER FROM:
PS/Chancellor to PS/Secretary of State
for Trade & Industry

Pse type for 25 day.

*Ms A Brimelow
PPS/Secretary of State for Trade + Industry*

Copies to:

PS/Secretaries of State for
Employment
Environment
Scotland
Transport
Energy

MINISTERIAL/NICG DINNER, 2 DECEMBER

The Chairmen would like to raise 3 topics for after dinner discussion on 2 December. I will circulate nearer the time some briefing which officials here are preparing.

2. First, they want to put the case for moving the control arrangements for those industries remaining in public ownership nearer to the private sector model. In particular, they are interested to gauge whether there is any Ministerial interest in making changes which, in their view, might ease the transition in due course of industries to the private sector. They have said that they do not want to revive the specific proposals they put forward in 1985 when the Nationalised Industries Bill was under discussion. But we understand that they do have in mind, for example, changes in capital structure.

3. Second, they want to discuss the European Community's plans for completing the internal market by 1992, particularly as they may bear on the UK public sector businesses. DTI and Treasury officials are already in contact with NICG representatives at working level. But the discussion at the dinner will give an opportunity to Ministers to hear what the Chairmen themselves have to say and to probe them on their purchasing policies.

4. Third, they want to float some ideas they are developing on how the Corporations might contribute towards the Government's policies on Inner City regeneration and

education and training. A number of the industries have experience in job creation activities, in training and in property development and they would like to make suggestions on how this experience might be put to good use in support of the Government's initiatives. They are not asking for extra money for this purpose.

5. I am sending copies of this letter to the ~~Private Secretaries to the Secretaries of State~~ ^{John Turner} for (Employment), ^{Robin Yarmy} (Environment), ^{Robert Gordon} (Scotland), ^{Roy Griffins} (Transport) and ^{Stephen Haddrill} (Energy).

{ JONATHAN TAYLOR }

JMT
P-S

FROM: I C R BYATT
DATE: 23 November 1987

CHIEF SECRETARY

cc Chancellor
Sir P Middleton
Mr Anson
Sir T Burns
Mr Monck
Mr Kemp
Mr Scholar
Mr Spackman
Mr Turnbull
Mr Cave

You will remember that during August Ministers agreed to the setting up of an Inter-departmental Group (of which I am Chairman) to review the discount rates and investment appraisal procedures in the public sector. Regular reviews of this kind were envisaged in the 1978 White Paper on Nationalised Industries. I think it likely that the review will lead to a recommendation to increase the rate in line with the increase in private sector profitability and in real interest rates since 1978.

2. A major part of the Group's work involves looking at the recent performance and practices of the private sector, as a useful guide to public sector procedures.

3. As part of this work I propose to arrange a small number of informal meetings with corporate planners and others working in the private sector to discuss what changes have occurred in private sector investment appraisal practices since the White Paper. The issues to be raised would include such things as how much investment is appraised, the techniques adopted, the level of the 'hurdle rate' which successful projects must pass, and the effects on the rate of the fall in inflation and tax changes.

4. The discussions would not be intended to provide a rigorous or representative answer to the questions posed, but would shed some light on how private sector practices are changing. I thought it would be useful to arrange meetings with NEDO's Committee on Industry and Finance, the Strategic Planning Society and possibly the Major Projects Association. Ideally the meetings would be held before Christmas.

5. These issues are of interest to the Treasury quite independently of the current review, and it would not be necessary to link our approach to the organisations with any announcement or indication that a review of the required rate of return (RRR) is in progress, or that it might result in a proposal to raise that rate. In view of the current debate about nationalised industry prices, it would not seem opportune to make such a disclosure at present.

6. The issues we would like to discuss are set out in the attached note. Can I take it that you are content for us to go ahead?

IB

I C R BYATT

AGENDA FOR MEETING WITH CORPORATE
PLANNERS, NEDO'S COMMITTEE FOR
INDUSTRY AND FINANCE ETC.

These questions are intended to throw light on private sector appraisal practices in general, rather than on procedures adopted by particular companies. The emphasis is on how practices have changed over the past ten or so years.

The Appraisal Process

Has there been a general change in the sequence of operations involved in investment appraisal (screening, definition, evaluation, decision)? For example, is more attention now allocated to any component.

To what degree are appraisal processes now more formalised?

Has the proportion of projects not subject to appraisal declined? If so, where has the change arisen?

Techniques

A range of techniques for investment appraisal is available (payback period, IRR, NPV, etc.). Has the balance of use among them changed? If so, in what direction?

Hurdle Rate

Are hurdle rates established typically

- a) pre-tax or post-tax,
- b) real or nominal?

How frequently are hurdle rates reviewed?

In such reviews, what factors are given most weight? For example, are they affected by changes in

- a) the weighted average cost of capital,
- b) risk-free interest rates,
- c) average rate of return by business,
- d) the expected or actual rate of inflation.

Has there been a change in the proportion of projects rejected?

Risk

How far is risk appraisal formalised, and how much importance is given to this aspect of the appraisal?

What formal methods are used? For example,

- a) an increase in the discount rate or reduction of the pay-back period,
- b) sensitivity analysis,
- c) probability analysis . . .

Ex post evaluation

Has there been an increase in the proportion of projects subject to ex post evaluation?

BF

~~14/10~~

Sarah

~~17/10~~

Not through with this yet! ~~18/10~~

Can you establish, from carbons,
whether ^{a copy} of X was attached to y?
[It shd have been!]

Moya

Yes!

Sarah

M

my

cc

PS/Chief Secretary
 PS/Financial Secretary
 Sir P Middleton
 Mr Anson
 Mr Monck
 Mr Burgner
 Mr Hawtin



Mr F K Jones
 Mr Gilhooly
 Mrs M E Brown
 Mr Colman Mr D Moore
 Mr M L Williams
 Mr Tarkowski
 Mr Call

Treasury Chambers, Parliament Street, SW1P 3AG
 01-270 3000

Ms A Brimelow
 PPS/Secretary of State for
 Trade and Industry
 1 Victoria Street
 LONDON
 SW1H 0ET

23/11/87
 23 November 1987

John Arlson

MINISTERIAL/NICG DINNER, 2 DECEMBER

The Chairmen would like to raise 3 topics for after dinner discussion on 2 December. I will circulate nearer the time some briefing which officials here are preparing.

First, they want to put the case for moving the control arrangements for those industries remaining in public ownership nearer to the private sector model. In particular, they are interested to gauge whether there is any Ministerial interest in making changes which, in their view, might ease the transition in due course of industries to the private sector. They have said that they do not want to revive the specific proposals they put forward in 1985 when the Nationalised Industries Bill was under discussion. But we understand that they do have in mind, for example, changes in capital structure.

Second, they want to discuss the European Community's plans for completing the internal market by 1992, particularly as they may bear on the UK public sector businesses. DTI and Treasury officials are already in contact with NICG representatives at working level. But the discussion at the dinner will give an opportunity to Ministers to hear what the Chairmen themselves have to say and to probe them on their purchasing policies.

Third, they want to float some ideas they are developing on how the Corporations might contribute towards the Government's policies on Inner City regeneration and education and training. A number of the industries have experience in job creation activities, in training and in property development and they would like to make suggestions on how this experience might be put to good use in support of the Government's initiatives. They are not asking for extra money for this purpose.



I am sending copies of this letter to John Turner (Employment), Robin Young (Environment), Robert Gordon (Scotland), Roy Griffins (Transport) and Stephen Haddrill (Energy).

Yours sincerely

Jonathan Taylor

J M G TAYLOR
Private Secretary

Ch/ I am extremely sorry it has taken so long to come back with the answer on X. DTI are content with suggestion, but

FROM: N MONCK

DATE: 3 December 1987

CHANCELLOR OF THE EXCHEQUER

Clarke to write. Letter for your signature behind. cc Chief Secretary Sir P Middleton Mr Anson Mr Byatt Mr Moore Mr Burgner Mrs Brown Mr Colman Mr M Williams Mr F K Jones Mr Tarkowski

Ch/ Shall we explore X?

YK

mpw 3/12

mpw

17/12

DINNER WITH THE NICG

I attach a record of the dinner on 2 December. It was a short discussion because you and Lord Young were delayed by a meeting until about 8.30 pm and you had to leave for a vote at 9.45. I attach a draft letter for you to send to Sir Robert Reid thanking him but also apologising for the chapter of accidents, which made the dinner short and led Messrs Ridley and Rifkind to be absent.

2. In para 2 of the draft letter I have included a square bracketed sentence suggesting a separate discussion about inner cities. This might be useful as well as diplomatic and it would be reasonable for Lord Young, as the senior Inner Cities Minister present at the dinner, to arrange it. But your private office would of course need to talk to him before including this in the letter.

3. I have also included at the end a sentence about returning the NICG's hospitality some time in 1988. You will want to consider whether to include it. It is certainly not operationally necessary and indeed may encourage NICG activity, whereas we would prefer to deal with individual industries about their particular problems if there are any and there is scope for action. But in the circumstances something of the sort would be diplomatic.

4. I also attach a draft Private Secretary letter designed to cover the record of the discussion, which ought to go round to sponsor departments, probably with copies of your letter to Bob Reid.

AM

N MONCK

RESTRICTED

NOTE FOR THE RECORD

MINISTERIAL/NICG DINNER : 2 DECEMBER

The Ministers present were the Chancellor, the Chief Secretary, Lord Young and Mr Cope for Employment. Mr Ridley and Mr Rifkind were not present. On the Nationalised Industries side those present were Sir Robert Reid (BR), Sir Bryan Nicholson (Post Office), Sir Philip Jones (Electricity Council), Mr Gordon Jones (Yorkshire Water and the Water Authorities Association), Sir Keith Bright (LRT) and Donald Miller (South of Scotland Electricity Board). Mr Driscoll (NICG director) was also present.

The Relationship between Government and Nationalised Industries and Control Arrangements

2. **Sir Robert Reid** said the Chairmen would like to discuss possible moves towards a private sector relationship in order to help prepare the industries more effectively for privatisation.

3. **Mr Gordon Jones** said the water industry was keen to be privatised but did not favour the National Rivers Authority taking on operational responsibilities or having 5,000 staff. **The Chancellor** replied that the NRA was necessary politically because privatising water was controversial. It would leave the water plcs free to concentrate on their core business and do their best for shareholders subject to regulation. The number of people employed by the NRA would depend to the extent to which its functions were contracted out.

4. **Sir Philip Jones** recognised that it was for Government to take the major decisions on electricity privatisation, but thought it essential for genuine dialogue with the industry to take place as soon as possible after those decisions. **The Chancellor** agreed that once the Government had taken its decisions, dialogue would be essential, though this would be easier for the Government to do the smaller the probability of leaks.

5. **Sir Philip Jones** said he was also concerned about the relationship between the Government and those nationalised industries which were likely to stay in the public sector for a long time. The private sector model was relevant, not just on EFLs, but on dividend control, capital structure, accounts and terms of service. **The Chancellor** replied that the private sector model was indeed the best one. But in practice it could not be aped: industries were either in the

private sector or not. This did not mean that changes were impossible within the public sector. There had been a lot of change, notably in the quality of top management, which was now far better than it was ten years ago, as the Chairmen would surely agree. **Lord Young** agreed, pointing out that nationalised industries could not be bankrupted, a key difference from the private sector.

6. **Sir Keith Bright** said he favoured bringing in more private sector disciplines (and also more dividends) and maximising the freedom to manage. **Sir Bryan Nicholson** said he favoured a common approach, so far as possible, which would define more clearly what the industries' management could do to help the Government. The **Chief Secretary** replied that he was doubtful about a common approach and that it was probably not in the interests of the industries themselves. He had been much more struck by the differences between the individual industries and their problems. He thought any changes in the control arrangements were likely to be gradual and differentiated between industries. **Lord Young** said this was well illustrated by the large differences between his three industries, the Post Office, British Shipbuilders and the British Steel Corporation.

The European Internal Market

7. The Chairmen asked for Ministers' views about the development of the internal market. **Lord Young** said he thought that Community decision making by qualified majority of voting was of great importance. The process of change, for example towards a common approach on public purchasing, would be a long one. There would of course be cheating, but the rules would gradually become established and this would lead to convergence after a lot of battles between governments on behalf of their national industries, and no doubt cases in the European Court of Justice. **The Chancellor** pointed out that there would be real gains to efficiency and for consumers from removing barriers. The strength of the pressures in that direction should not be underestimated.

Inner Cities

8. **Sir Keith Bright** said that the nationalised industries could offer management, property and goodwill, as well as training capacity. The industries wished to discuss what they could do to help the Government in the inner cities.

9. At this point Ministers had to leave for a vote.



N MONCK

HM Treasury

3 December 1987

pl type final
for Ch/EX signature

DRAFT LETTER FOR THE CHANCELLOR TO SEND TO SIR ROBERT REID ^{CBE}

(M)

Many thanks for having my colleagues and me to dinner. ~~[last week.]~~ I am sorry that in the event, for a number of reasons beyond our control, we were with you for such a short time and that some of my colleagues were at the last moment unable to come.

2. In the short time available I thought we had a useful discussion on two of the important subjects you raised. ~~(I hope that we will be able to arrange a separate discussion of the third one, the contribution which the nationalised industries might make in the inner cities. (I will be getting in touch with you about that.)~~ ^{at some stage} ^{Kenneth Clarke} ~~David Young~~

3. It was good to meet you and your colleagues again. I hope that we will be able to return your hospitality some time during 1988.

[NL]

**DRAFT LETTER FROM CHANCELLOR'S PRIVATE SECRETARY TO LORD YOUNG'S PRIVATE
SECRETARY**

NICG DINNER FOR MINISTERS

I enclose a record of the discussion at this dinner on 2 December. I am sending copies to [Mr Cope's Private Secretary] and to the Private Secretaries of those sponsor Ministers who were not able to be present [Energy, Transport, Environment, Scotland].



Treasury Chambers, Parliament Street, SW1P 3AG

01-270 3000

17 December 1987

Sir Robert Reid CBE
Nationalised Industries Chairmen's Group
Hobart House
Grosvenor Place
LONDON
SW1X 7AE

Alan

Many thanks for having my colleagues and me to dinner. I am sorry that in the event, for a number of reasons beyond our control, we were with you for such a short time and that some of my colleagues were at the last moment unable to come.

In the short time available I thought we had a useful discussion on two of the important subjects you raised. I hope that at some stage we will be able to arrange a separate discussion of the third one, the contribution which the nationalised industries might make in the inner cities. Kenneth Clarke will be getting in touch with you about that.

It was good to meet you and your colleagues again. I hope that we will be able to return your hospitality some time during 1988.

NIGEL LAWSON

Alan
Nigel



Treasury Chambers, Parliament Street, SW1P 3AG
01-270 3000

17 December 1987

Sir Robert Reid CBE
Nationalised Industries Chairmen's Group
Hobart House
Grosvenor Place
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NIGEL LAWSON

*Yours
Nigel*

215 5147

NAT. Ind
pmp

cc CST
 Sir P Middleto
 Mr Monck
 Mr Anson
 Mr Byatt
 Mr Moore
 Mr Burgner
 Mrs Brown
 Mr Colman
 Mr M Williams
 Mr F K Jones
 Mr Tarkowski

Treasury Chambers, Parliament Street, SW1P 3AG
 01-270 3000

17 December 1987

Jeremy Godfrey Esq
 Private Secretary to the
 Secretary of State for Trade and Industry

Dear Jeremy,

NICG DINNER FOR MINISTERS

... I enclose a record of the discussion at this dinner on 2 December.

I am sending copies to Bob Ledsoe (Employment), Stephen Haddrill (Energy), Jon Cunliffe (Transport), Robin Young (Environment), David Crawley (Scottish Office) and Alastair Morgan (Chancellor of the Duchy's Office)

Yours
Moira

MOIRA WALLACE
 Assistant Private Secretary

RESTRICTED

NOTE FOR THE RECORD

MINISTERIAL/NICG DINNER : 2 DECEMBER

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9. At this point Ministers had to leave for a vote.

M

N MONCK

HM Treasury

3 December 1987

Nationalised Industries' Chairmen's Group

~~RRR~~
pwp

Chairman
Sir Bryan Nicholson

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

CHIEF SECRETARY	
REC.	17 JAN 1989
ACTION	Mr Byatt
COPIES TO	Cx, Sir P Middleton Mr Anson, Mr Manick, 16 th January 1989 Mrs Lomax, Mr Beestall Mr Call

Hobart House
Grosvenor Place
London SW1X 7AE
01-235 2020

Dew John,

When my colleagues and I met in December, considerable concern was expressed about Press reports that Treasury officials were planning changes to the measure of "the opportunity cost of capital" - the concept introduced in the 1978 white paper on the Nationalised Industries and which the Corporations use when judging the return on investment programmes.

I should make it clear that the concerns were not addressed to the requirement itself to earn returns sufficient to match or exceed the opportunity cost of capital. The concept was accepted as a reasonable one in discussions with the then Chancellor in 1978 and we remain of that view.

Nor was there any disposition at our meeting to suggest that the specific order of quantity of the rate of return cannot be altered from time to time as circumstances change.

Our anxieties were directed to the fact that officials may have done a considerable amount of work on re-assessing the proper current level of the opportunity cost of capital without letting the Group know that the exercise was under way, nor consulting it about the calculations involved or the implications of any figures emerging.

Against that background my colleagues have asked me to put two requests to you. The first is that we should be told whether there is a reassessment in progress, and if the answer to that is affirmative, our second request is for an assurance that we shall be involved in the exercise, and given an adequate opportunity to express our views before a decision is reached.

Of equal importance to our Industries are the "rules of the game" within which any new figure might subsequently be applied; and whether the present rules are likely to be developed in any way. In this respect I understand that whilst in 1978 Ministers and Chairmen alike blessed the "opportunity cost of capital" concept in general, Chairmen had reservations about the practicality of aspects of the RRR system and consequently Ministers went no further than saying that its possible development was still under discussion. As far as we know that remains the formal position.

I have a meeting of the NICG Advisory Committee on the 27th of this month and it would be helpful to have a response in time for that meeting.

Yours sincerely,
Bryan

28/188

[Handwritten signature]
46/2

FROM: I C R BYATT
DATE: 20 January 1989

PS/Chancellor
Re Peter Middleton

COPY FOR

CHIEF SECRETARY

[Handwritten notes in red ink: "copy into (Whom?)", "appoint", "to a trustee"]

cc
Mr Monck
Mrs Lomax
Mr Beastall
Mr Moore
Mr Bent
Mr Houston

LETTER FROM THE NICG ON THE RRR

Sir Bryan Nicholson wrote to you on 16 January concerning the level of the required rate of return for nationalised industries and other public sector trading bodies.

2. You will remember that we reviewed the level of public sector discount rates last year and that the results of the review were submitted by Sir Peter Middleton to the Chancellor in August. The Chancellor subsequently wrote to colleagues. Since then there has been some discussion at Permanent Secretary level and we hope to have the matter settled relatively soon. We would then propose to announce the outcome of the review in the answer to an arranged PQ.

3. There was however in December a leak - after the papers had left the Treasury - and short articles in both the Financial Times and the Independent referring to the 8% RRR and, in the case of the Financial Times, the 6% rate for the non-trading services. Not surprisingly this was picked up by the NICG Secretariat who view everything the Treasury do with the deepest suspicion. The determination of a new number for the RRR also takes them back to old battles. They have always agreed that, in principle, the nationalised industries should earn as good a rate of return on new investment as the private sector but in practice they have been chary of mechanisms designed to achieve this result.

4. The letter which Sir Bryan Nicholson sent you represents a compromise between different parties in the NICG. I am told that Sir Philip Jones, aided and abetted by NICG officials wants to make a fuss. Others for example Mr Sellers, Chairman of the NICG

Finance Panel, recognise that the RRR ought to be raised and did not want to write a letter all.

5. On substance, we cannot concede their request for involvement in the determination of the RRR. The choice of a public sector discount rate has always been the matter for Government, as part of our responsibility for the overall management of the economy. When the chips are down, most NICG members will not dispute this. The attached draft is designed to make this point while being as soothing as possible on what we are doing now and in relation to old battles.

6. Sir Bryan Nicholson asks for a reply by 27 January. Mr Monck and I think that it is desirable to reply before then. A reply timed to arrive on 26 January would seem appropriate.



I C R BYATT

Draft Reply to Sir Bryan Nicholson

Thank you for your letter of 16 January.

2. I can confirm that we have indeed been reassessing the level of the opportunity cost of capital. The judgement, in 1978, that it should be 5% in real terms before tax was based principally on the pre-tax returns which have been achieved by private companies and the likely trend in the return on private investment. Since then, there has been a big increase in the real rate of return achieved by the private sector. The figures are set out in the Autumn Statement indicate the real rate of return earned by industrial and commercial companies is now over 11%. We confidently expect that levels of profitability will continue to be well above those achieved in the second half of the 1970s and the first half of the 1980s.

3. I am glad to see from your letter that you and your colleagues are not querying the requirement for nationalised industries to earn returns sufficient to match or exceed the opportunity cost of capital or the case for charging the required rate as circumstances change. The judgement on the number, which is based on the macro economic performance of the private sector, must rest with the government, as it has responsibilities for the management of the economy as a whole. While the evidence clearly points to a significant increase, we think it right to adopt a cautious approach. Although it would be possible, on the basis of private sector returns to justify doubling the existing number of 5%, a smaller increase, to something of the order of 8%, seems appropriate in current circumstances. We would, as in the past, review this number from time to time.

4. The industries would however certainly be involved in discussing the practical consequences of a change in the number. There would be no impact on pricing during the life of existing financial targets. Such targets will remain the primary expression of the financial performance which the Government intends the industries to achieve. The RRR will, as now, be an important factor in determining new financial targets, but the targets will also depend on other factors such as the earning power of existing assets. We would of course continue to consult the corporations about the level and phasing of new financial targets.

5. A change in the RRR would obviously influence the appraisal of individual investment projects. But, as at present, the choice of discount rate for appraising individual projects is a matter for each nationalised industry to decide in consultation with sponsor departments and the Treasury. In such discussions the Government's main concern will continue to be that the industry's approach should be compatible with achieving the RRR on the investment programme as a whole. In appraising whether or not new capital investment projects should be undertaken, proper allowance will need to be made for risk. The effect of a full allowance for risk may be implicitly equivalent to requiring a higher internal rate of return on riskier projects. I understand that some corporations make use of discount rates in excess of the RRR.

6. As you will see, none of this involves any change in what you call "the rules of the game" and the discussions envisaged would mean that corporations would be involved in working out all the practical consequences of a decision to raise the RRR.

7. The prospect of privatisation raises issues which were not considered in 1978. Particularly where they are appraising investment with long expected lives, the

corporations will want to take full account of the costs they are likely to face in rising capital in private markets. In current circumstances these costs appear to be well in excess of 5% in real terms, although the exact number will depend on the circumstances of the industry and the state of the markets as well as on factors specific to individual investment projects.

8. I hope these points are helpful. We would of course let you and other Chairmen know in advance of any announcement about our review.

Nationalised Industries' Chairmen's Group

pwp

Hobart House
Grosvenor Place
London SW1X 7AE

01-235 2020

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

CHIEF SECRETARY	
REC.	- 7 FEB 1989
	Mr Manck
TO	Mr Sin P. Meddellon
	Mr Anson, Mr Byatt
	Mr Lomax, Mr Beattall
	Mr Call.

6th February 1989

Dear John,

OPPORTUNITY COST OF CAPITAL

Thank you for replying so promptly to my query about the reports of impending changes in the measurement of the opportunity cost of capital, since that allowed me to sound the views of my colleagues when we met recently.

On the main point in your letter, ie., that the public sector businesses should henceforth take 8% rather than 5% as the current measure of the opportunity cost of capital, we have no substantial comment to offer. Corporations will, of course, take due note of that guidance, along with all other relevant considerations, when they come to make their decisions on the shape of their future investment programmes and on what Test Discount Rates they will use to appraise individual investment projects. Similarly, they will expect these issues to be raised, again along with all other relevant considerations, when the time comes for sponsor Departments to approach them about the setting of new Financial Targets - which we are happy to see remain as the primary measure of the financial performance which the Government expects our businesses to achieve.

I should add, however, that without questioning that the decision is yours to take, colleagues were concerned about the fact that you have taken it without giving the Chairmen the opportunity to contribute their tuppence-worth to your deliberations. This was of course the central point which I put to you, at my colleagues' request, in my letter of 16th January.

Yours sincerely
Byatt

FROM: D J L MOORE - PE
DATE: 4 December 1989
EXTN: 4440

PS/CHANCELLOR

Content f

cc PS/Chief Secretary
Sir P Middleton
Mr Anson
Mr Monck
Mr C W Kelly
Mr Bent
Mrs Brown
Mr F K Jones
Mr M Williams
Mr S Wood
Mr Judge
Mrs Chaplin

Ch/ Content for me to write as drafted? We can't stop the NICG raising any subject they like, and - with the exception of the environment - there are all old chestnuts. So is pay, on our side.

NICG DINNER

TT

The Chancellor and other Ministers are dining with a selection of Nationalised Industry Chairmen on 11 December. It is the practice on these occasions for an agenda to be agreed for after pudding discussion, and for you to circulate Treasury briefing to the other Ministers coming.

2. I attach a draft letter for you to send to your opposite numbers advising them of the items which the NICG would like to raise: latest ideas on the privatisation programme and on policy towards ongoing nationalised industries; environmental policy; policy towards the EEC and purchasing rules in particular.

3. I have told Mr Driscoll that we have advised Ministers to raise the 1990 pay scene in discussion. I have also said that Ministers will be briefed on each of the three items the NICG have suggested though it is for the Chairmen to decide where their priorities lie. They have been told that Ministers are likely to leave to vote at 10 o'clock and so obviously there is limited time for discussion. I have given Driscoll my personal view that they will not be learning anything new about the privatisation programme.

DJM

D J L MOORE

pse type
lined

DRAFT LETTER FROM:

PS/CHANCELLOR

TO:

C Novis Esq,
PS/Secretary of State for Employment

Coxon House
Tothill

NICG DINNER

The Chancellor, your Secretary of State and other Ministers are dining with the NICG on 11 December. Julie Thorpe's letter of 28 November listed the Chairmen coming and gave details of the arrangements.

In after dinner discussion the Chancellor would like to spend a little time talking about prospects for the 1990 pay scene. For their part, the NICG have suggested the three following items:

(a) The content and timing of the privatisation programme, and policy toward the still nationalised corporations.

- They may raise here the use of private sector funding and we are told that Mr Collier may want to talk about the level of infrastructure expenditure, although it is far from clear precisely what he has in mind.

(b) Environmental policy.

- The Chairmen are interested in the Secretary of State for Environment's views on this; Sir Robert Haslam (Coal) is particularly concerned with how any measures might impinge on his industry.

(c) Policy towards the EEC.

- Their particular interests are the steps being taken to create a single market and, within that, the proposed "excluded sectors" purchasing rules.

Treasury officials have advised the NICG that Ministers will be briefed on each of these three items. The Chairmen know that Ministers may have to leave to vote at 10pm and so they will need to consider where their priorities lie in the limited time available. They may let us know on Friday afternoon what is their preferred order for discussion, after pay in 1990.

I aim to circulate by the weekend briefing prepared here on each of the four items. The sponsor Minister concerned will no doubt deal with questions raised on particular industries.

I am sending copies of this to the Private Secretaries to Mr Ridley, Mr Parkinson, Mr Wakeham, Mr Patten, Mr Forsyth and Mr Lamont.

~~TANCRED~~ TARKOWSKI

djlm

FROM: D J L MOORE - PE
DATE: 7 December 1989
EXTN: 4440

PS/CHANCELLOR

cc PS/Chief Secretary
Sir P Middleton
Mr Anson
Mr Monck
Mr Bent
Mr Williams
Mr Judge
Mrs Chaplin
Without attachments:
Mrs M E Brown
Mr F K Jones
Mr S Wood
Ms E Young

NICG DINNER

I understand that you have sent the letter attached to my note of 4 December. I would be grateful if you would send the recipients of that letter the four briefs attached. They have been prepared by the Treasury Groups concerned.

We will let you have tomorrow very short notes on each of the Chairmen attending. They will be for the Chancellor and the Chief Secretary, and not for onward transmission.

djlm

D J L MOORE

pkj

FROM: F K JONES
DATE: 7 December 1989

PS/CHANCELLOR

cc PS/Chief Secretary
Sir P Middleton
Mr Anson
Mr Monck
Mr D J L Moore
Mr Bent
Mr M L Williams
Mr Judge
Mrs Chaplin

NATIONALISED INDUSTRIES' CHAIRMAN'S GROUP

I attach a revised version, agreed with Mr McIntosh, of the brief which he sent to you earlier today. There is a change in the second indent in the note on the Single Market, and some revisions in the piece on Public Procurement.

KJ.

F K JONES

Covering CONFIDENTIAL



Treasury Chambers, Parliament Street, SW1P 3AG
01-270 3000

7 December 1989

C Norris Esq
PS/Secretary of State for Employment
Department of Employment
Caxton House
Tothill Street
LONDON
SW1H 9NA

cc PS/Chief Secretary
Sir P Middleton
Mr Anson
Mr Monck
Mr D J L Moore
Mr C W Kelly
Mrs M E Brown
Mr Bent
Mr F K Jones
Mr M Williams
Mr S Wood
Mr Judge
Mrs Chaplin

See above,

NICG DINNER

... My 5 December letter promised that we would circulate briefing on each of the items which the NICG have suggested for discussion after dinner. This is attached.

We have since heard that the Chairmen may not, after all, wish to raise (c) "Policy towards the EEC". Since we have already prepared a brief, this is included in case the subject is, after all, raised.

I am sending copies of this letter to Neil Thornton (DTI), Roy Griffins (DTP), John Neilson (DEN), Roger Bright (DOE), David Binnie (Scottish Office) and Carys Evans.

Tomasz Tarkowski
T TARKOWSKI
Private Secretary

CONFIDENTIAL

NICG DINNER, 11 DECEMBER : PAY ISSUES

Points to make

- Pay rising too fast throughout economy. Especially important that pay increases are justified by underlying increases in productivity. Unit costs are already rising faster than in all our major competitors. Control of unit costs vital for competitiveness of industry. Must get this right.
- Know you are aware of need for pay increases to be properly targeted on areas (whether by region or by skill) where you have difficulties of recruitment and retention. This is no doubt part of your thinking when you set objectives and strategies. Very helpful if you can provide information on recruitment and retention position in your industries, both across the board and for particular groups, when making proposals on pay.
- Sure you recognise need for Ministers to bear in mind possible repercussive effects which pay increases in one nationalised industry can have on others, and on rest of public sector.
- A housekeeping matter : hope you are all now aware that the notice you need to give of your pay proposals before you make a first offer has been extended to 14 working days. This will give sponsor Ministers a little more time to consider your proposals. Once negotiations are underway we recognise you may not be able to give so much warning. But would be helpful if you could give us as much notice as possible of revised proposals.

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Questions to put

Ministers may wish to ask the Chairmen:

- (i) how they see the pay scene in their industries over the next year;
- (ii) how they plan to use their paybill more effectively in order to bring down their unit costs;
- (iii) what increased flexibilities they have in mind for their pay systems which will enable recruitment and retention problems to be more precisely targeted and addressed.

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PRIVATISATION PLANS

1. The priority is to privatise the Electricity industry in the lifetime of this Parliament. This means a succession of major sales in the second half of 1990 and the first of 1991 [NB Ministers have not yet announced a decision on when the Scottish Boards will be sold within this period]. In addition, the Post Office should complete the sale of Girobank shortly and the Scottish Bus Group will be privatised through 11 trade sales in 1990.

2. After the Election:

- already announced that Coal will be sold; no decision yet on whether it will be as a whole or in parts;

- depending on the outcome of current studies, British Rail may be privatised; again no decision yet on whether as a whole or in parts.

3. Of the other major industries:

- no plans yet for the Post Office; privatisation of Royal Mail ruled out in this Parliament.

- London Buses: to be privatised and deregulated in due course.

- London Underground: no plans for the time being.

- British Waterways Board: DOE/Treasury Ministers considering Board's proposals for future strategy.

- Civil Aviation Authority: looking in particular at options for future management of national air traffic control services.

ON-GOING NATIONALISED INDUSTRIES

4. For those industries with no early prospects for privatisation, the aim is to continue the policy of improving their performance as efficient businesses within the public sector - and, thanks to the effort of Chairmen and their Boards, excellent progress has been made in meeting this objective over the last few years.

5. But while they are within the public sector the present broad framework of financial controls must remain - external financing limits and three year plans; financial and performance targets.

6. The Treasury and the sponsor department are always ready to look at questions of, for example, capital structure of individual industries. But it is not useful to look at this in terms of general solutions for the industries. The remaining nationalised industries each have their very distinctive characteristics and problems and it is sensible to look at their individual needs.

7. The Government is not in the business of cutting capital investment. On the contrary, the 1989 Public Expenditure Review allowed for some very large increases for several of the industries. But before approving programmes the Government has to be satisfied that the investment will earn an adequate return and that it is part of a realistic and manageable programme.

8. The Government continues to welcome ideas for involving private finance - eg through the joint venture British Rail are now negotiating for the Channel Rail Link. But we have to be satisfied that it is cost effective and, for example, that the risks are genuinely transferred to the private sector and that the private sector partners are bringing something to the party through new ideas and skills.

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BRIEFING FOR NICG: ENVIRONMENT

Points to Make

1. Environment issues are very wide-ranging. Some are essentially about the quality of life in the UK alone (certain short-range pollution issues; planning policy); others affect neighbouring countries (acid rain, North Sea clean-up); still others are of global significance (the greenhouse effect and the ozone layer).
2. The Government's Environment Bill is directed at the reform of our pollution control systems. It will establish a framework for regulation to deal with a range of pollutants, up to those of global significance.
3. The wider issues are being considered in international negotiation, since no one country can solve them by itself. Significant progress has already been made on SO₂ and Nox emissions.
4. The global issues will come to a head over the next year, with the London conference reviewing the Montreal protocol on the protection of the ozone layer (likely to focus on CFCs, halons, methyl chloroform and carbon tetrachloride) in June and the world climate conference in November 1990. Much work remains to be done before then.
5. Among the matters on the international agenda are possible targets for greenhouse gas emissions, and regulation and market measures to deliver these. But it is essential to consider these in a co-ordinated fashion, with full and proper analysis.

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6. In considering the UK's approach on such matters we will want to be sure that we do not undermine competitiveness; that the most cost-effective solutions are chosen; and that adjustment cost is kept to a necessary minimum.

7. We are clear that these objectives and measures must be consistent with continued economic growth, to produce resources for combating pollution. Prime Minister made this point in her speech to UN General Assembly on 8 November.

Background

8. The principal nationalised industries concerned with environmental issues are British Coal, and the electricity supply industry, (and the Atomic Energy Authority), who are most interested in the implications for energy pricing and regulation of or charging for polluting emissions, and British Rail, who see themselves as a relatively "clean" transport technology which should be favoured by comparison with their road and air transport competitors.

9. The NICG are likely to press for clarification of where the Government stands on these issues. They are aware of Mr Patten's recent speeches, in which he has advocated use of the market to achieve environmental goals and suggested that market prices, notably of energy, ought to reflect full long-run marginal costs, including environmental costs. Mr Wakeham has indicated sympathy with this as a possible way forward. They will also be aware of the November 1989 Conference at Noordwijk in the Netherlands, where the UK joined the majority which declared itself in favour of stabilising greenhouse gas emissions by the year 2000, on a basis to be agreed at the world climate conference next year.

10. The coal and electricity industries are likely to press for clarification of what this means for prices and outputs of British and imported coal, methane gas and oil. Of these fossil fuels, coal produces the greatest emissions of greenhouse gases per unit of energy. The possibility of increased coal prices is of

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particular concern to the chairmen: to the coal industry in relation to its competitive position (and the level of future Government support); and to the electricity industry, which may find its endowment of coal-fired plant leaves it in a weak commercial position after privatisation. BR has a different perspective, and may press for higher taxes on road fuel, lower investment in roads, and higher rail investment.

11. At this stage, the Government is still considering its approach. These issues will be considered by MISC 141, under the Prime Minister's chairmanship. This Committee is setting an exacting work programme, to meet the timetable set by the programme of international negotiations in the Inter-Governmental Panel on Climate Change (IPCC) leading to the World Climate Conference in November 1990, and by the Government's commitment to produce a wide-ranging White Paper on environmental issues in November next year. In principle, the Government is prepared to join its partners in negotiating an international convention on climate change, and in pursuit of objectives agreed in negotiation to employ a range of measures, making use as appropriate of regulation and market measures to deliver the agreed objectives. The Government is clear that such objectives and measures should be consistent with continued economic growth.

12. At this stage, it would be difficult to be specific in response to the expected line of questioning. The main points to make are those given above. You can assure the chairmen that their specific concerns will be taken into account in further work.

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POLICY TOWARDS THE EC
SINGLE MARKET: GENERAL

Line to take

- Single Market programme on target. Over half of the measures agreed. But still much to be done: UK will keep up pressure on the Commission and the Presidency.

Background

The Single Market programme consists of nearly three hundred measures to remove remaining barriers to free movement of goods, services, capital and people within the European Community by the end of 1992.

Over half the programme has been agreed (152 measures to date), although few measures have yet been implemented in all member states.

Areas of particular interest to the nationalised industries will include:

- (i) the removal of barriers to public procurement (see attached brief);
- (ii) the harmonisation of technical standards of manufactured goods;
- (iii) opening up of financial services, especially banking - where important measures have been agreed which will allow free access to services across national borders; and
- (iv) mutual recognition of professional qualifications to free up the supply of skilled workers in the Community.

PUBLIC PROCUREMENT

Line to take

1. Opening up procurement is a single market priority. British suppliers stand to benefit. The directive will protect purchasers from possible interference in the future.
2. Any measure like this involves some burdens for those who do not need the rules. We cannot expect to get rules that apply only to countries where purchasing is on nationalistic lines.
3. The Government has aimed to reduce the burdens to a minimum. The proposal is now much less bureaucratic than it was. Purchasers should think of the rules as a framework: more can be done within them than may be realised: purchasers need to ensure that their procedures are consistent with the rules in order to avoid risk of challenge under the expected enforcement directive.
4. Unfortunate that UK ideas for testing procurement systems (instead of applying detailed rules) were not adopted. But interest in testing persists, and the subject is worth pursuing in the medium term.
5. If necessary: the need is now to get a common position if we can. We do not know how the issues will come out. But we understand that the German coal sector claims it should be treated on a par with upstream operations. This has in the end to be a political decision.
6. If necessary: the Commission's original proposal on standards was unacceptable. But the provision as it now is it should not put obstacles in the path of purchasers who can justify their need to impose special requirements.
7. Grateful for help given to officials in work on the Commission's proposal.

Background

Nationalised industries are affected by the intention to introduce rules on public procurement outside the Government sector. The Internal Market Council may reach a common position on an intended directive on 21-22 December. The Commission's proposal - which covers water, energy, transport and telecommunications - aims to prevent political interference in purchasing by imposing a framework of rules for the award of contracts. The nationalised industries claim that they buy competitively already and that the imposition of rules impedes their progress on the path to commercial behaviour on which the Government has set them.

While the Government has accepted the principle of applying rules to nationalised industries and their successors, and also to companies such as British Gas and BT, it has aimed to exclude "upstream" oil and gas (exploration and extraction). It may prove successful in this, in return for accepting conditions on the Government's relations with the operators. But it will be touch and go, and another part of the price may be letting German and Spanish coal be exempted in the same way. (They appear to fit the conditions for exemption which the Commission has devised for upstream oil and gas.) British Coal is concerned about the imbalance within the coal sector that would result.

The Government, with backing from the CBI and the NICG, has argued that undertakings which submit their procurement systems to independent costs, and perform satisfactorily in them, should not have to follow the detailed rules. This has not been accepted, and there is no chance of it being included in the common position. But the idea of testing (or 'audit') is being taken up by the Commission in a proposal it is about to make on enforcement.

Ministers have still to decide on the UK's position on the directive in the form that it now is.

Officials have had regular meetings on the procurement proposal with representatives of the NICG, usually including Mr Driscoll, its Director.

Sir Robert Reid has recently written to the Chancellor, Mr Ridley and Mr Wakeham on the proposal.

RESTRICTED

BF 19/12 (NB below)

PPS PL

FROM: N MONCK
DATE: 13 December 1989
EXT: 4399

PS/CHANCELLOR

cc PS/Chief Secretary
PS/Paymaster General
PS/Sir P Middleton
Mr Anson
Mr Phillips
Mr Edwards
Mr Kelly
Mr Moore
Mr Bent
Mrs M E Brown
Mr F K Jones
Mr O'Donnell
Mr M Williams
Mr S Wood
Ms Young
Mrs Chaplin

NICG DINNER

I attach a short note of the general discussion at the dinner.

IM

2. I suggest you send copies to the private secretaries of the Ministers who were present and Mr Rifkind under a minimal covering letter:

[

"NICG DINNER

I attach a record of the general discussion of the dinner on 11 December. The Chancellor has written to Sir Bryan Nicholson thanking him for the NICG's hospitality on behalf of Ministers.

I am sending copies to the private secretaries of the other Ministers who were present as well as Mr Rifkind's."

NB

I understand that your office is arranging the thank you letter.

3. I attach a cutting from the Independent today reporting that the Chancellor spoke about pay. Neither the NICG secretariat nor the Treasury press office can throw any light on the source for the first two paragraphs.



N MONCK

RESTRICTED

DISCUSSION AT DINNER GIVEN FOR MINISTERS BY THE NATIONALISED
INDUSTRY CHAIRMEN'S GROUP : 11 DECEMBER

Present

Chancellor

Secretary of State for Trade and Industry

Secretary of State for Transport

Secretary of State for Energy

Secretary of State for Environment

Chief Secretary

Sir Bryan Nicholson (NICG and Post Office)

John Collier (Atomic Energy Authority and Nuclear Electric)

Sir Robert Haslam (British Coal)

David Ingman (British Waterways Board)

Sir Philip Jones (Electricity Council)

Michael Joughin (North of Scotland Hydro-Electric Board)

Sir Robert Reid (British Rail)

Christopher Tugendhat (Civil Aviation Authority)

1. The general discussion covered only pay and the environment.

Pay

2. The Chancellor referred to the worsening pay situation and the crucial importance of focussing on productivity so as to keep unit costs down and of targeting large increases precisely on skills or geographical areas in which there were recruitment or retention problems. The Chairmen should provide information on these when they consulted sponsor Ministers about pay negotiations; consultation should take place fourteen days in advance of the initial offer. The inevitable acceleration of later stages made the provision of this information initially even more crucial. Ministers were bound to be concerned about repercussions of pay increases in individual industries. The Secretary of State for Employment said that the growth of earnings had obstinately refused to go significantly below 7 per cent in any of the widely varying economic situations experienced in recent years. The UK's unit labour costs were clearly now rising faster our competitors'.

3. Sir Robert Reid said the industries had to respond to the labour market. In the south east vacancy rates were commonly around 25 per cent and this was bound to have an effect on service quality. The Chairmen recognised the need to keep basic increases to the minimum and to target higher increases carefully.

Sir Philip Jones said that the private sector was in the lead this year, setting a "base line" of the order of 9½ per cent. Ministers' advice last year to delay settlements until inflation came down had not been borne out by experience.

Sir Bryan Nicholson said that there was increasing diversity within individual nationalised industries. The Post Office now had a differential rate in London and the south east. It had been agreed that local increases could be made without negotiation or national balloting whenever a formula related to local unemployment and attrition rates was triggered. The industries had to pay enough to "stay in the game" so that they could recruit and restore service quality if the labour market slackened.

Sir Christopher Tugendhat said that earlier arguments about the repercussions of increases for specialist CAA employees on Post Office pay had not seemed to him to be convincing.

4. The Chancellor said that the possibility that unemployment might begin to rise again allowed the industries to trade on the greater security of jobs in the public sector. They should deny the relevance of a going rate or of the RPI which might move unevenly as he had told the House of Commons. They could also stress that excessive pay increases could threaten quality by reducing investment. It was vital to prevent pay increases rising to a level at which they would go out of control. Possible unrest in the industries was a lesser risk than allowing that to happen.

The Environment

5. Sir Philip Jones said that the Chairmen, having read press reports of Ministerial discussions, would very much like to hear Ministers' views about the trade off between environmental protection and economic growth and about the extent to which other countries would "play fair". He felt that progress on the environment would require more explicit transport and energy policies than we had now. If Ministers were to ask the industries to include an environmental section in their corporate plan, would they get a response?

6. The Secretary of State for Environment said that progress on the environment was not wholly or mainly a matter for the DOE. But it was important to find a robust intellectual basis for environmental policy, particularly because of the international meetings in 1990 on the ozone layer and global emissions. The UK Government would have a particular contribution to make on the use of the price mechanism and market forces and would want to ensure that the UK's international competitiveness did not suffer. He saw no paradox in supporting both economic growth and environmental protection. But hard decisions would be needed. There was also a growing market in clean technology and a risk that the UK share of this business would fall. The Secretary of State for Transport agreed that there could often be more money where there was less muck. There was scope for emphasising increased miles per gallon in cars rather than speed per second.

7. Sir Robert Haslam stressed the large potential impact of environmental policies on the coal industry and the scope for improving energy efficiency in electricity generation. Sir Robert Reid commented that tunnelling under London to make railways more acceptable was a very high cost option which would make no money. Completing the link to the Channel tunnel was justified not by saving a few minutes on the journey between London and Paris but in order to have adequate rail capacity three years after the tunnel opened.

8. The dinner ended a little before 10 o'clock when Ministers had to vote.

N Monck

HM Treasury
13 December 1989

Wednesday, December 13, 1989

THE INDEPENDENT

Major warns on public sector pay

By Michael Harrison
Industrial Editor

THE CHANCELLOR of the Exchequer, John Major, has warned nationalised industry chairmen to clamp down hard on wage settlements next year to prevent a pay explosion undermining the fight against inflation.

His warning, delivered to heads of Britain's state-owned industries at a private dinner, suggests that the public sector is in for another bruising round of wage bargaining next spring which may provoke a repeat of this year's rail, tube and postal strikes.

The dinner on Monday night was hosted by Sir Bryan Nicholson, chairman of the Post Office, and attended by a large number of the 12 nationalised industry chairmen, who include Sir Robert Reid of British Rail, Sir Philip Jones of the Electricity Council, Sir Robert Haslam of British Coal and Wilfred Newton of London Regional Transport.

At least three Cabinet ministers, including the Transport Secretary, Cecil Parkinson, and the Financial Secretary to the Treasury, Norman Lamont, also attended.

Prior to this year's wage round the Treasury instructed nationalised industry chairman to limit pay rises to 7 per cent. In the event virtually all the big state industries settled above the rate of inflation after a wave of debilitating industrial action in key services. BR's 128,000-strong

workforce accepted 8.8 per cent, Post Office workers settled for 8 per cent and electricity workers received 9.2 per cent.

Friday's inflation figures are expected to show a rise in the retail price index to around 7.8 per cent, while pay settlements are ranging between 7.5 and 10 per cent. The Treasury is forecasting that inflation will remain above 7 per cent in the first six months of next year but fall to 5.75 per cent by the fourth quarter, suggesting that Mr Major is pressing the public sector to peg wage rises at around 7 per cent again.

However, Alastair Hatchett, of Incomes Data Services, warned that the Post Office, BR and London Regional Transport may face pressure to concede higher pay awards to overcome problems of recruiting and retaining staff.

The series of big private sector wage settlements due in January may also put upward pressure on state industry pay claims.

According to the Confederation of British Industry, pay settlements in manufacturing averaged 8.3 per cent in the third quarter compared with 7.6 per cent in the second quarter. ICI workers have settled for 9.6 per cent while Ford is offering 9.5 per cent and Vauxhall 9.7 per cent.

Christ



Handwritten signature

Treasury Chambers, Parliament Street, SW1P 3AG
01-270 3000

20 December 1989

C Norris Esq
PS/Secretary of State for
Employment
Department of Employment
Caxton House
Tothill Street
LONDON
SW1H 9NA

cc PS/Chief Secretary
Sir P Middleton
Mr Anson
Mr Monck
Mr Moore
Mr C W Kelly
Mrs M E Brown
Mr Bent
Mr F K Jones
Mr M Williams
Mr S Wood
Mr Judge
Mrs Chaplin

Dea Cive,

NICG DINNER

... I attach a record of the general discussion of the dinner on 11 December. The Chancellor has written to Sir Bryan Nicholson thanking him for the NICG's hospitality on behalf of Ministers.

I am sending copies to the private secretaries of the other Ministers who were present as well as Mr Rifkind's.

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Private Secretary

RESTRICTED

DISCUSSION AT DINNER GIVEN FOR MINISTERS BY THE NATIONALISED
INDUSTRY CHAIRMEN'S GROUP : 11 DECEMBERPresent

Chancellor

Secretary of State for Trade and Industry

Secretary of State for Transport

Secretary of State for Energy

Secretary of State for Environment

Chief Secretary

Sir Bryan Nicholson (NICG and Post Office)

John Collier (Atomic Energy Authority and Nuclear Electric)

Sir Robert Haslam (British Coal)

David Ingman (British Waterways Board)

Sir Philip Jones (Electricity Council)

Michael Joughin (North of Scotland Hydro-Electric Board)

Sir Robert Reid (British Rail)

Christopher Tugendhat (Civil Aviation Authority)

1. The general discussion covered only pay and the environment.

Pay

2. The Chancellor referred to the worsening pay situation and the crucial importance of focussing on productivity so as to keep unit costs down and of targeting large increases precisely on skills or geographical areas in which there were recruitment or retention problems. The Chairmen should provide information on these when they consulted sponsor Ministers about pay negotiations; consultation should take place fourteen days in advance of the initial offer. The inevitable acceleration of later stages made the provision of this information initially even more crucial. Ministers were bound to be concerned about repercussions of pay increases in individual industries. The Secretary of State for Employment said that the growth of earnings had obstinately refused to go significantly below 7 per cent in any of the widely varying economic situations experienced in recent years. The UK's unit labour costs were clearly now rising faster our competitors'.

3. Sir Robert Reid said the industries had to respond to the labour market. In the south east vacancy rates were commonly around 25 per cent and this was bound to have an effect on service quality. The Chairmen recognised the need to keep basic increases to the minimum and to target higher increases carefully.

Sir Philip Jones said that the private sector was in the lead this year, setting a "base line" of the order of 9½ per cent. Ministers' advice last year to delay settlements until inflation came down had not been borne out by experience.

Sir Bryan Nicholson said that there was increasing diversity within individual nationalised industries. The Post Office now had a differential rate in London and the south east. It had been agreed that local increases could be made without negotiation or national balloting whenever a formula related to local unemployment and attrition rates was triggered. The industries had to pay enough to "stay in the game" so that they could recruit and restore service quality if the labour market slackened.

Sir Christopher Tugendhat said that earlier arguments about the repercussions of increases for specialist CAA employees on Post Office pay had not seemed to him to be convincing.

4. The Chancellor said that the possibility that unemployment might begin to rise again allowed the industries to trade on the greater security of jobs in the public sector. They should deny the relevance of a going rate or of the RPI which might move unevenly as he had told the House of Commons. They could also stress that excessive pay increases could threaten quality by reducing investment. It was vital to prevent pay increases rising to a level at which they would go out of control. Possible unrest in the industries was a lesser risk than allowing that to happen.

The Environment

5. Sir Philip Jones said that the Chairmen, having read press reports of Ministerial discussions, would very much like to hear Ministers' views about the trade off between environmental protection and economic growth and about the extent to which other countries would "play fair". He felt that progress on the environment would require more explicit transport and energy policies than we had now. If Ministers were to ask the industries to include an environmental section in their corporate plan, would they get a response?

6. The Secretary of State for Environment said that progress on the environment was not wholly or mainly a matter for the DOE. But it was important to find a robust intellectual basis for environmental policy, particularly because of the international meetings in 1990 on the ozone layer and global emissions. The UK Government would have a particular contribution to make on the use of the price mechanism and market forces and would want to ensure that the UK's international competitiveness did not suffer. He saw no paradox in supporting both economic growth and environmental protection. But hard decisions would be needed. There was also a growing market in clean technology and a risk that the UK share of this business would fall. The Secretary of State for Transport agreed that there could often be more money where there was less muck. There was scope for emphasising increased miles per gallon in cars rather than speed per second.

7. Sir Robert Haslam stressed the large potential impact of environmental policies on the coal industry and the scope for improving energy efficiency in electricity generation. Sir Robert Reid commented that tunnelling under London to make railways more acceptable was a very high cost option which would make no money. Completing the link to the Channel tunnel was justified not by saving a few minutes on the journey between London and Paris but in order to have adequate rail capacity three years after the tunnel opened.

8. The dinner ended a little before 10 o'clock when Ministers had to vote.

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HM Treasury

13 December 1989