Part. H.

SECRET

(Circulate under cover and notify REGISTRY of movement)

DECLASSIFIED
AK
5-11-14

Begins: 5/3/85
Ends: 29/10/87.

PO -CH /NL/0246
PART A

PO -CH /NL/0246
PART A

Chancellor's (Lawson) Papers:

THE COAL INDUSTRY AND PRIVATISATION'

Disposal Directions: 25 Years

26/9/95.

AR
5-11-14

CHANCELLOR OF THE EXCHEQUER

C/

Although not classified "personal", the last sentence indicates this has been written as a personal letter.

It's clearly sensitive but I don't think it would do harm to circulate it internally on a selective basis, if you're content

OK – on a more very selective basis. 7/3

1 have much sympathy provided the people are worth the salary.

2. How do NEB Board salaries now compare with other N/Is?

8

NATIONAL COAL BOARD
HOBART HOUSE
GROSVENOR PLACE
LONDON SW1X 7AE

01-235 2020

CHAIRMAN
Ian MacGregor

5th March, 1985.

The Rt. Hon. Nigel, Lawson, MP,
Chancellor of the Exchequer,
11 Downing Street,
London,
S.W.1.

Dear Chancellor,

Salaries of Full-time Board Members

When I came to take up my present post with the National Coal Board I saw it as one of my principal tasks to establish an effective organisation at Board level capable of bringing about the improvements of which I know the coal industry is capable.

In part, this has involved a careful personal appraisal of the senior management within the industry and I am pleased to say that I have been encouraged by the quality of many of the senior people I find here. I believe it will be possible in most, if not all cases to bring to the fore people capable of taking over the major tasks in the future. At the same time, however, I do not rule out the possibility that some management skills might, at some time, have to be brought in from outside.

One aspect of the task which remains to be dealt with, however, is the structure of rewards for those who have to bear the responsibility. While I was at BSC I was pleased to be able to make some progress in overcoming the long-standing problems of creating a worthwhile career path to Board level. I am writing now to seek your support to the same end at the National Coal Board.

I am sending to the Secretary of State for Energy a formal proposal to establish a new salary range for full-time Members of the Board which will go some way to overcome the existing lack of incentive for outstanding people to aspire to take on Board Member jobs. I stress in that submission - of which I enclose a copy - that the proposal represents the joint view of myself and the external non-executive Members of the Board, who have wide experience in many sides of industry and commerce. We are united in the view that a really significant increase in the salary range for Board members would be one of the most valuable messages that the Government could convey to the management of the coal industry as evidence of the determination to create a really efficient national asset.

4001/3/85/B/021/MS

I stress this point because I fear that arguments over the details of the proposal could distract from the really essential point that any improvement must be substantial enough to be seen as the beginning of a new approach towards the management of the industry.

I hope you will forgive my writing to you this personal letter and that you will understand the importance I and the non-executive Members of the Board place on this decision.

Sincerely,

Ian MacGregor.

4001/3/85/B/022/MS

AK

~~CONFIDENTIAL~~

NATIONAL COAL BOARD

BOARD MEMBERS' SALARY RANGES

Memorandum by the Remuneration Committee

Salary Ranges for Full-Time Board Members

The personal salaries of full-time Board Members have been increased by 5.2% with effect from 1st November 1983 and a further 5.2% from 1st November 1984. It was agreed that the issue of salary ranges should be left for separate consideration. The present full-time Members (other than the Chairman and Deputy Chairman) who were on the maximum of the November 1982 range each now have personal salaries of £44,800.

In the past, full-time Board Members recruited from within the industry have normally come from among the senior officials in Senior Grades 1 and 2 (Directors-General, Area Directors and some other equivalent posts). Officials in those grades have, in turn, normally been responsible to full-time Board Members for the activities of their Department or formation. Thus, there has always been a close working relationship between the two groups, but there is a clear difference in both legal and functional responsibility and therefore a need for an appropriate and significant salary differential.

The present salaries are:-

Full-Time Board Member	£44,800
Senior Grade 1	£35,058 to £44,379
Senior Grade 2	£33,134 to £41,947

Since most officials who are likely to be promoted to the Board from SG1 are on their range maximum, the salary differential between them and the full-time Board Members (in some cases to whom they report directly) is at present less than 1%.

The effect of this lack of salary differential has been to enforce the use of personal salaries towards the top of the relevant range maximum in

W/D85/23/MAR

order to provide a financial incentive to accept promotion. This lack of differential has existed since the end of the main pay restraint period in the mid-1970's, and is shown in Annex 1, which also shows the stability in real terms of the salaries of senior officials over that period.

The inevitable result of appointments being made high within the relevant range is that there is very little scope to use the ranges effectively, either in providing adequate headroom for increments based on performance, or in providing varying initial salaries within the range to reflect the weight of a particular post and the worth of the postholder.

If the November 1982 Board Members' salary range were to be updated to November 1984 using the percentage increases given on personal salaries, the resultant range, £35,560 to £44,800, would be virtually identical to that of officials in Senior Grade 1. Accordingly it is our view that it is essential that an entirely new range be agreed in order that salary determination for Board Members can be put on a sensible and workable footing at the earliest possible moment. This new range must also have regard to the external industrial and commercial market for comparable posts. (It is to be noted that this was the basis of the similar exercise by British Telecom after privatisation).

These views are confirmed by the report of a recent confidential survey (the results of which are available only to subscribing members of the CBI) which shows that the salaries of full-time Board Members and the Deputy Chairman of the National Coal Board lie almost at the bottom of the range of salaries paid for jobs of comparable size in a representative group of 154 public and private sector organisations surveyed in November 1984.

There appear to us to be two alternative approaches to determining a new salary range with appropriate differentials: either (i) to restore the range in real terms to that which applied in the period (in 1972) when there was a satisfactory differential; or (ii) to create a new range based on provision of a suitable differential over the current salaries for subordinate levels of management.

(i) Restore the 1972 Differential:

The Board Members' salary range implemented with effect from January 1972, following the first report by the Top Salaries Review Body, was £12,000 to £17,000. This range gave an appropriate differential as the range maximum for Senior Grade 1 was, with effect from July 1971, £10,750. To restore this differential at November 1984 price levels would give a Board Members' range of:

£49,527 to £70,163: say in round terms £50,000 to £70,000.

(ii) Create a New Basis for Salary Differentials:

Alternatively a new range could be created with a differential at Board Member minimum over Senior Grade 1 maximum of 20%. In order to give adequate scope for recognition of experience, merit and performance, it is suggested that the maximum of the Board Member range should be set 50% above the minimum. This would give a range of:

£53,255 to £79,883: say £53,000 to £80,000.

Having established a new range for full-time Board Members, it is important that it should be maintained at the correct level and we would propose that the range minimum should normally be held at a minimum of 20% above the maximum of the Senior Grade 1 range.

Deputy Chairman

With the establishment of a new salary range for Board Members, it will be necessary for the salary range for the Deputy Chairman to be reviewed to ensure an appropriate differential.

W/D85/25/MAR

The last approved salary range for the Deputy Chairman was £39,550 to £50,055 with effect from November 1982. The increases agreed since then for Board Members would give a notional range from November 1984 of £43,770 to £55,400.

In fact it has been necessary for the Deputy Chairman to be paid a salary higher than the range maximum since July 1983. At present it remains at this level of £56,500, although it became open for review with effect from January 1985.

To re-establish a Deputy Chairman range with the differential appropriate to the two cases suggested above would give the following:-

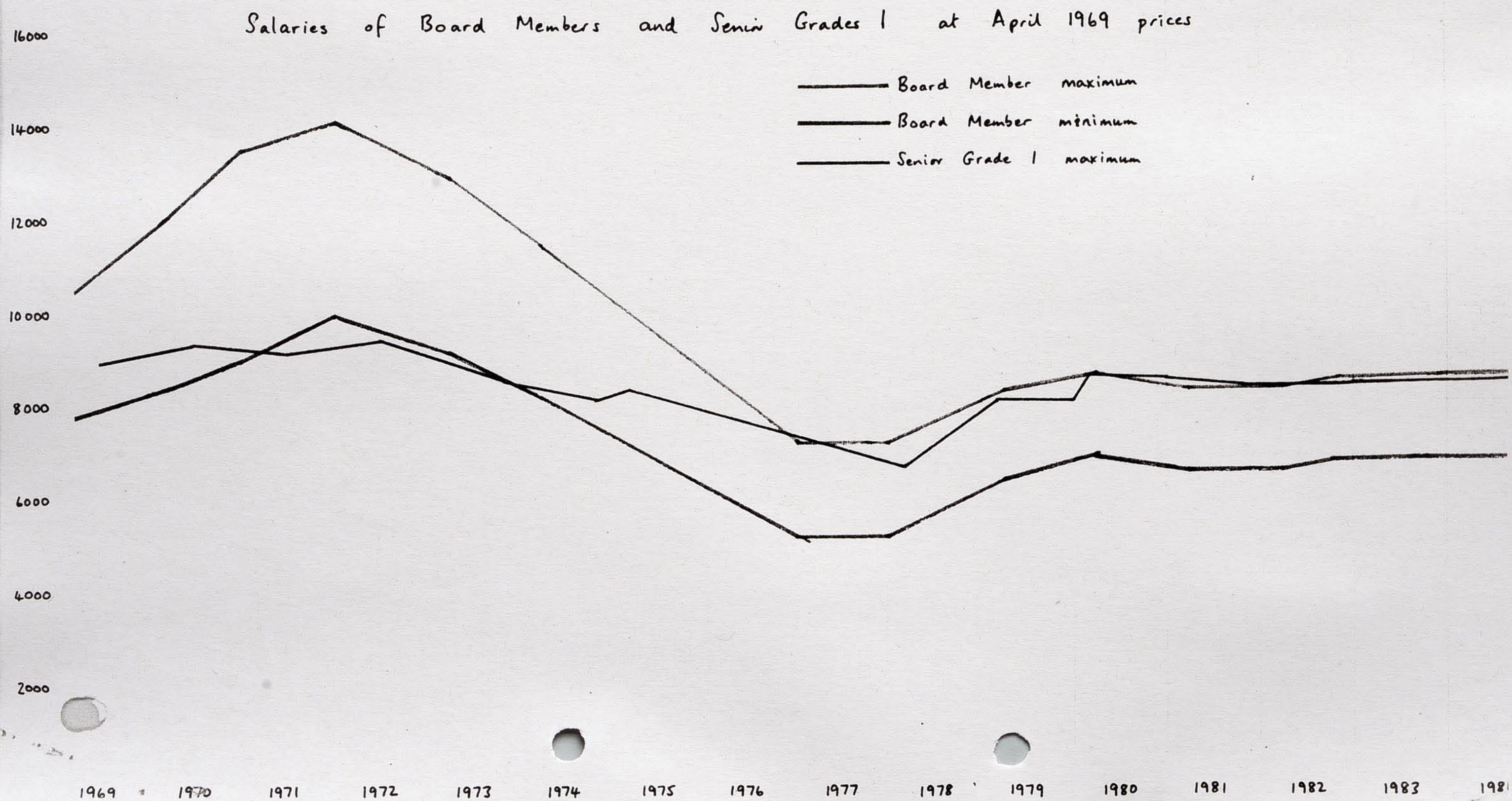
(i)	Board Member	£50,000	to	£70,000
	Deputy Chairman	£67,500	to	£85,000
(ii)	Board Member	£53,000	to	£80,000
	Deputy Chairman	£77,000	to	£97,000

Conclusions

Of the two cases suggested above we would would favour case (ii) for consideration. If it were felt that these represent too large an immediate increase, we would favour the increase being made in not more than two stages.

W/D85/26/MAR

ANNEX 1



Salaries of Board Members and Senior Grades 1 at April 1969 prices
Board Member maximum
Board Member minimum
Senior Grade 1 maximum
16000
14000
12000
10000
8000
6000
4000
2000
1969
1970
1971
1972
1973
1974
1975
1976
1977
1978
1979
1980
1981
1982
1983
198

c/ Letter to issue?
MOM 19/3

PERSONAL & CONFIDENTIAL

Pse fix a private mtg with Mr M. This is better than writing — & wd also enable him to raise one or 2 other matters. N.

AK

FROM: T U BURGNER
14 March 1985

CHANCELLOR

cc: Sir Peter Middleton
Mr Monck

NCB: SALARIES OF FULL-TIME BOARD MEMBERS

Mr MacGregor has written to you enclosing proposals, also sent to Mr Walker, for a new salary structure for NCB Executive Board members and Deputy Chairman. You may like some comments - those below are partly on the general context and partly on the proposals themselves. I have discussed the letter with Mr Monck but not with anyone at the Department of Energy since there is no indication that Mr Walker knows of this approach to you.

2. By substantially increasing the differential between Board salaries and the maximum of the staff grade immediately below Board level, Mr MacGregor's aim is to create "a worthwhile career path to Board level". He recognises the proposals which are agreed with the non-executive Board members amount to "a really significant increase in the salary range", but stresses the need for the Government to send a clear message of their interest in creating an efficient coal industry and a new approach to the industry's management.

3. The proposals are of course for Mr Walker to consider in the first instance. He may well be unaware that you have been approached. Mr MacGregor's aim appears to be to try to ensure that when Mr Walker consults you you will be favourably disposed.

4. Current Board salary levels are:

Board member	£44,800
Deputy Chairman	£56,500 (unchanged since 1983).

For comparison the level immediately below the Board is paid in a range £35,058 to £44,379 so there is virtually no differential between the maximum of the top staff range and the Executive Board salary.

5. Mr MacGregor puts forward two alternatives for the Board as follows:

Either	- Board members	£50,000-£70,000
	- Deputy Chairman	£67,500-£85,000

These ranges are based on restoring differentials with senior staff that existed in January 1972 following the first TSRB report.

<u>Or</u>	- Board member	£53,000-£80,000
	- Deputy Chairman	£77,000-£97,000

A new range which would create a differential of 20 per cent between the <u>maximum</u> of the staff range and the <u>minimum</u> of the Executive Board range. The intention would be to maintain the differential at this level.

6. Some comments on these proposals:

(i) While NCB salaries are of course well below large (profit-making) private sector organisations, they are not particularly low by the standards of other large nationalised industries. The table attached shows some comparisons. The NCB's position is slightly worse if the performance bonuses for BSC and the Post Office are added.

(ii) Mr MacGregor's proposals involve extremely large increases - at Board member level the range amounts to a 12-57 per cent increase under his first proposal, 18-79 per cent under his second. Normally we would contemplate increases of this order only if it was judged essential to recruit or retain some particularly valuable <u>individual</u>. You will have your own views on the argument that it is desirable to send a message of this kind to the NCB. Certainly it is an argument that we can expect to hear repeatedly - usually at the Treasury's expense - in the aftermath of the strike. As for the other arguments used - the comparison with comparable posts in the private sector, the reference to BT after privatisation, and the confidential CBI salary survey - these are very like arguments used by other nationalised industry Boards and we would normally not attach much weight to them.

(iii) Miss O'Mara's minute noted that you were sympathetic to Mr MacGregor's approach provided that those concerned were worth the salary. It would be important to establish who exactly Mr MacGregor intends should be paid on these scales. The Press have had a number of reports of possible imports from the coalfields to the Board - Eaton, Moses and Wheeler have all been mentioned. It would not be surprising if people in their positions needed a fairly handsome differential to tempt them to Hobart House.

(iv) Accepting percentage increases of anything like this level will sit uncomfortably with your general approach to Board pay on which there will be an E(NI) discussion soon after the Budget. We will be advising you there to give as little ground as possible to colleagues who will be pressing you for larger increases for their Boards generally.

see separate folder

(v) Apart from the hike to the minimum, the proposals both involve wide ranges which are intended to reward responsibility and performance. We have never much liked ranges and prefer to see performance directly reflected in a performance-related bonus scheme. (Mr MacGregor introduced one for BSC; one has been agreed for the Post Office and there are discussions for BAA). The NCB might well be a suitable candidate for such a scheme. It would also make a large increase more easily defensible.

(vi) Mr MacGregor's second proposal is objectionable on general grounds. By creating a fixed differential between Board and senior staff salaries it would allow the Board effectively to determine their own salary levels. Ministers would have to be told and might need to become involved in pay for senior NCB staff.

(vii) Mr MacGregor suggests that his second proposal, which involves even bigger increases, might be in two stages. Staging would be almost inevitable for increases as large as either of his proposals.

7. There is no need for you to get involved in the detail of this until Mr Walker writes to you on these or some other proposals. But you will clearly want to reply to Mr MacGregor's letter. It may be wise to signal some of the problems in these proposals even if in very general terms. I attach a draft.

TB

T U BURGNER

Encs: 6 (top only)
2 (others)

CONFIDENTIAL

Board	Members £	Deputy Chairman/ Chief Executive £	Chairman £
National Coal Board	44,800	56,500*	59,325*
British Gas Corporation	35,210-44,690	43,535-55,100	66,500
Central Electricity Generating Board	35,370-44,555	43,535-59,950	66,500
Electricity Council	35,370-44,555	43,535-55,100	66,500
British Shipbuilders	34,425-37,500	47,500	86,000 (excluding performance bonus)
British Steel Corporation (excluding performance bonuses)	41,675-52,260	65,000	110,000 (annual equivalent)
Post Office (excluding performance bonuses)	46,800-52,500	56,000	63,000
British Rail	39,250-44,000	52,500 (annual equivalent)	66,800

The lowest figures actually paid to Board members in the gas, electricity and steel industries are above the minimum of the ranges shown (BGC £40,695; CEGB £42,715; Electricity Council £42,715; BSC £48,600 excluding bonus).

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*1983 salaries

Pl. type

DRAFT LETTER FROM CHANCELLOR OF EXCHEQUER TO:
Ian MacGregor Esq
Chairman, National Coal Board

address below

~~CONFIDENTIAL~~ AK

SALARIES OF FULL-TIME BOARD MEMBERS

You wrote to me on 5th March, ~~and attached~~ enclosing a paper [about] with proposals for a new salary structure for full-time members of your Board. It is of course for Peter Walker to deal with ~~this~~ these in the first instance but I thought you might like to have ~~an~~ my initial reaction.

2. I have considerable sympathy with your general aim of creating a worthwhile/career path to Board level. Nevertheless, as you clearly recognise, the increases under either of your proposals - even with staging - are very substantial. [It is vitally important in the interests of promoting employment and competitiveness in the economy that we] We must achieve low pay settlements generally, if we are to promote employment and competitiveness in the economy. Against that background I have to be cautious in agreeing large increases for nationalised industry Boards, however well justified. It is particularly difficult when the increases apply to the Board as a whole rather than to individuals of outstanding merit, although the position might be eased slightly if increases in pay were combined with reductions in the size of the Board itself. And there is the risk that Some of the arguments you use in relation to the NCB might be thought by other nationalised industry Boards to apply equally in their case.

3. [I should like to put one further point to you.] One further point occurs to me. While you were at BSC, you put forward proposals for a performance-related bonus scheme for the Board. This has now been [in operation] operating successfully for over a year. BSC was the first nationalised industry to [come up with] produce a scheme of this kind, although other nationalised industries are now following down this road. As a means of rewarding individual merit, a performance-related bonus scheme coupled with personal salaries could substitute for the very wide salary ranges you have in mind. It ~~is~~ would also be a good deal easier to defend large increases publicly if they ~~are~~ could be explicitly related to performance in this way.

4. I am copying this letter to Peter Walker

[N.L.]

CONFIDENTIAL

NATIONAL COAL BOARD
HOBART HOUSE
GROSVENOR PLACE
LONDON SW1X 7AE

01-235 2020

CHAIRMAN

Ian MacGregor

3rd December, 1985

~~IN CONFIDENCE~~ AK

Rt. Hon. Nigel Lawson MP,
Chancellor of the Exchequer,
Treasury,
Parliament Street,
London, SW1P 3AG.

Dear Nigel,

When we met last week I promised to send you a copy of the latest position on redundancies in the current financial year, our progress with closures in the same period and also an analysis of the industry's results for October. These are enclosed together with a comparison sheet of results for the September 1983 period from which you will readily see that we are making substantial progress to turning this industry round into an efficient business.

Sincerely,

Ian.

3037/12/85/L/043/AJP

SECRET

NATIONAL COAL BOARD

APPENDIX IX

COLLIERIES

ACTUAL RESULTS - CUMULATIVE TO SEPTEMBER, 1983

		SCT	NEA	NYK	DCR	BNY	SYK	NDY	NNT	SNT	SMD	WES	SWL	GB
Revenue Saleable Output	'000 tnes	2812	5821	4130	2916	3547	3407	3376	5706	3538	3281	5027	3437	46998
Overall Shifts	000's	1474	2580	1266	1293	1354	1430	1124	1733	1373	1395	1912	2208	19142
OMS - Production	tnes	7.72	9.61	13.94	8.00	12.14	12.35	10.05	13.61	9.30	10.65	14.66	7.02	10.51
OMS - Overall	tnes	1.91	2.26	3.26	2.25	2.62	2.38	3.00	3.29	2.58	2.35	2.63	1.56	2.46
EMS - Overall	£	30.47	33.23	35.59	31.33	34.59	33.67	34.25	34.18	33.22	33.83	33.01	30.39	33.01
Saleable Realisations	per tne £	38.75	39.24	36.63	39.46	39.11	40.70	36.68	39.15	36.92	36.12	40.47	45.57	39.10
		£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
FINANCIAL RESULTS														
Net Proceeds		109.1	223.6	149.2	115.8	139.5	138.8	128.9	222.1	133.1	120.5	201.1	157.9	1839.5
Costs														
Wages		44.4	82.1	44.9	40.4	44.8	47.2	37.9	59.0	45.6	47.1	62.8	62.6	618.8
Wages Charges		21.7	37.2	17.8	19.0	18.5	19.6	15.2	24.4	19.5	20.4	26.6	32.3	272.2
Materials, Repairs and MCW		23.5	46.2	27.2	21.0	23.4	23.2	22.6	37.0	22.7	25.0	41.7	28.8	342.3
Other Colliery Expenses		10.8	26.4	16.1	8.9	27.3	12.6	17.2	17.7	18.5	10.2	16.6	27.5	209.9
Non Operational Expenses		15.8	23.7	17.1	15.9	17.0	17.1	14.9	20.8	15.1	17.2	23.7	21.8	220.0
Power, Heat & Light, Plant Hire, Deprec.		22.8	42.2	29.3	23.3	27.3	24.5	23.7	39.8	23.4	25.4	40.9	32.6	355.2
Total Costs		139.0	257.8	152.4	128.5	158.3	144.2	131.5	198.7	144.8	145.3	212.3	205.6	2018.4
SEPTEMBER PERIOD		(3·5)	(0·7)	(0·2)	(3·1)	(8·4)	(0·1)	–	6·5	(1·8)	(6·3)	(2·6)	(7·3)	(27·5)
OPERATING PROFIT/(LOSS)- as per APPENDIX I		(29.9)	(34.2)	(3.2)	(12.7)	(18.8)	(5.4)	(2.6)	23.4	(11.7)	(24.8)	(11.2)	(47.7)	(178.9)

Note : Individual entries may not sum to total because of rounding.

COSTFORM19,1&2(WPX1)

SECRET

T AR

NATIONAL COAL BOARD

APPEND

COLLIERIES

ACTUAL RESULTS - CUMULATIVE TO OCTOBER 1985

		SCT	NEA	NYK	SYK	NDY	NOTTS	SMD	KENT	WES	SWL			GB
REVENUE SALEABLE OUTPUT	000 TNES	2,332	5,336	7,594	6,427	3,390	10,143	3,239	210	5,215	3,608			47,495
OVERALL SHIFTS	000 S	1,097	2,470	2,720	2,585	1,172	3,264	1,156	191	1,938	2,110			18,703
O.M.S. - PRODUCTION	TNES	9.63	10.09	14.15	11.64	9.54	11.52	12.11	7.50	15.28	7.39			11.23
O.M.S. - OVERALL	TNES	2.13	2.16	2.79	2.49	2.89	3.11	2.80	1.10	2.69	1.71			2.54
E.M.S. - OVERALL	£	32.20	34.62	36.66	34.25	37.39	37.92	38.60	35.11	35.97	33.01			35.68
SALEABLE REALISATIONS	PER TNE £	39.04	41.36	40.21	42.37	37.59	41.40	37.26	55.03	43.25	47.15			41.37
TOTAL COSTS	PER TNE £	54.75	49.49	47.59	45.45	45.74	40.34	42.73	90.29	47.23	62.27			47.12
		£M	£M	£M	£M	£M	£M	£M	£M	£M	£M	£M	£M	£M
FINANCIAL RESULTS														
NET PROCEEDS		92.7	238.9	309.9	273.4	127.0	419.6	121.2	11.8	228.6	176.7			1,999.7
COSTS														
WAGES		35.3	81.6	96.4	87.7	43.2	122.9	44.5	6.7	69.4	65.2			652.9
WAGES CHARGES		18.6	38.5	40.3	40.6	15.8	49.0	18.0	3.6	29.0	32.1			285.7
MATERIALS, REPAIRS AND M.C.W.		22.7	44.9	59.1	46.5	30.4	72.3	22.8	2.4	49.0	32.6			382.7
OTHER COLLIERY EXPENSES		9.5	26.5	55.0	25.0	21.2	38.0	10.2	.8	20.9	32.2			239.2
NON OPERATIONAL EXPENSES		18.0	26.6	40.6	37.1	17.1	43.7	18.1	1.9	28.3	24.2			255.5
POWER HEAT & LIGHT, PLANT HIRE, DEPREC.		23.5	46.1	70.0	55.3	27.3	83.2	24.8	3.6	49.7	38.3			421.8
TOTAL COSTS		127.7	264.1	361.4	292.1	155.1	409.1	138.4	19.0	246.3	224.7			2,237.8
OCTOBER PERIOD		(2·4)	2·6	(3·5)	2·6	(1·5)	7·6	0·6	0·3	(0·9)	(3·8)			1·7
OPERATING PROFIT/(LOSS)- PER APPENDIX 1		(35.0)	(25.2)	(51.5)	(18.7)	(28.1)	10.5	(17.2)	(7.2)	(17.7)	(48.0)			(238.1)
CAPITAL CHARGE		(10.8)	(13.6)	(85.0)	(24.0)	(9.8)	(35.3)	(13.2)	(1.6)	(23.5)	(12.2)			(229.0)
SUB TOTAL		(45.8)	(38.8)	(136.5)	(42.7)	(37.9)	(24.8)	(30.4)	(8.8)	(41.2)	(60.2)			(467.1)
OTHER MINING ACTIVITIES ETC.		40.9	2.[illegible]	2.7	1.3	0.1	1.9	0.6	0.[illegible]	1.8	1.5			52.6
OPERATING P/(L)-AFTER CAP CHARGES		(4.9)	(36.7)	(133.8)	(41.4)	(37.8)	(22.9)	(29.8)	(8.4)	(39.4)	(58.7)			(414.5)

FORM F 339

REDUNDANCY 1985/6: MEN OFF BOOKS AND MEN STILL ON NOTICE AS AT 29TH NOVEMBER 1985

			REDUNDANCY										TOTAL REDUNDANCY AS % AGE OF START YEAR M.O.B.
			OFF BOOKS YEAR TO DATE			CURRENTLY UNDER NOTICE			TOTAL REDUNDANCY				
	START YEAR M.O.B.	CURRENT M.O.B.	-50	50+	TOTAL	-50	50+	TOTAL	-50	50+	TOTAL		
MEN ON COLLIERY BOOKS													
SCT	11263	8561	1522	998	2520	180	102	282	1702	1100	2802		24·9
NEA	21913	19478	848	1314	2162	331	577	908	1179	1891	3070		14·0
NYK	25967	22278	160	3212	3372	253	1045	1298	413	4257	4670		18·0
SYK	25947	20977	[illegible]28	34[illegible]3	4021	1119	997	2116	1647	4490	6137		23·7
NDY	10059	9562	19	483	502	8	170	178	27	653	680		6·8
NOTTS	27537	27104	—	625	625	—	235	235	—	860	860		3·1
SMD	10103	9679	75	413	488	103	152	255	178	565	743		7·4
KENT	2242	1458	297	439	736	—	—	—	297	439	736		32·8
WES	17055	16389	17	591	608	172	217	389	189	808	997		5·8
SWL	19293	16368	947	1370	2317	1008	1036	2044	1955	2406	4361		22·6
GB	171379	151854	4413	12938	17351	3174	4531	7705	7587	17469	25056		14·6
"OTHERS" WITHIN AREA CONTROL	11636	10362	392	1016	1408	113	377	490	505	1393	1898		16·3
NATIONAL WORKSHOPS	6552	4590	[illegible]3	[illegible]4	1557	30	203	233	703	1087	1790		27·3
NATIONAL STORES	599	523	12	39	51	14	8	22	26	47	73		12·2
N.C.B. (COAL PRODUCTS) LTD.	3989	3388	264	310	574	55	9	64	319	319	638		16·0
								OVERALL TOTAL	9140	20315	29455		
								CHANGE ON PREVIOUS WEEK		+	617		

[IN ADDITION, AREAS HAVE, ACTING AS AGENTS, GIVEN NOTICE TO A FURTHER 18 MEN AT REGIONAL ETC LOCATIONS OUTWITH THEIR CONTROL AND NOT COVERED ABOVE]

9. The summarised position is:-

(i)

Collieries	No.	Output 1983/4 ('ooo tonnes)	Current Manpower	Manpower Change Year to Date
Closures to date	21	5,718	7,451	-4,747
Agreed locally	5	1,860	2,656	-502
Referred to I.R.B.:	2	1,297	1,796	-865
Subject to National Appeal:				
Meeting held, awaiting Board decision	2	469	1008	-435
Meeting yet to be held	2	614	756	-942
Other closures announced	1	262	344	-76
TOTAL	33	10,220	14,011	-7,567
		Output affected ('000 tonnes)		
Other action	24	1,622	24,059	-5511
GRAND TOTAL	57	11,842	38,070	-13,078

(ii) Workshops

Workshops	No.	Current Manpower	Manpower Change Year to Date
Closures to date	7	39	-1,697
Rationalisation	1	20	-41

(iii) Stores

Closures announced	1	29	-3

(iv) Coal Products

	No.	Current Manpower	Manpower change year to date
Closures to date	3	100	-195
Agreed locally	2	440	-85
Other action	4	1,348	-273

~~SECRET~~ AK

BRIEF FOR THE MEETING OF THE EXECUTIVE COMMITTEE

2ND DECEMBER, 1985

Closures and Other Action to Reduce Activity

1. The attached tables set out the detailed position on closures and other action to reduce activity. One colliery was closed last week - Haig (the colliery was working on a "development only" basis and operations ceased with Union agreement on 26th November, 1985).

2. Elsecar workshops and Caerphilly Tar Plant also closed last week (on 29th November, 1985).

3. The NUM have withdrawn their appeal locally on the merger of North Gawber with Woolley. All three Unions have now agreed the merger.

4. The NUM at Kinsley have voted (80%/20%) in favour of opposing the proposed closure.

5. The NUM at Fryston have voted (on 29.11.85) to accept closure. NACODS had already agreed closure.

6. The Unions at Horden held meetings at the weekend.

7. There will be a Reconvened Review Meeting on Garw this week.

8. The 3 outstanding appeal meetings are:

Polkemmet	NUM/NACODS
Betteshanger	BACM
Woolley (partial)	NUM/NACODS

~~SECRET~~

COLLIERY CLOSURES

CLOSED TO DATE:

COLLIERY	DATE OF CLOSURE	MANPOWER AT CLOSURE	CURRENT MANPOWER
BRENKLEY	25:10:85	477	477
SACRISTON	15:11:85	212	212
HERRINGTON	22:11:85	561	561
ACKTON HALL	5:7:85	503	44
SAVILE	23:8:85	289	63
YORKSHIRE MAIN	11:10:85	1180	1169
CORTONWOOD	25:10:85	691	691
BROOKHOUSE	25:10:85	581	580
MOORGREEN	19:7:85	321	111
PYE HILL	9:8:85	468	-
BOLD	15:11:85	704	704
HAIG	26:11:85	162	162
WOLSTANTON	18:10:85	633	633
BEDWAS	31:8:85	32	-
CELYNEN SOUTH	6:9:85	349	222
MARKHAM	20:9:85	456	175
TREFOREAN	30:9:85	6	3
ABERPERGWM	7:10:85	358	358
PENRIKYBER	8:10:85	512	507
ABERTILLERY	9:10:85	445	411
ST JOHNS	22:11:85	368	368
TOTAL 21		9308	7451

AGREED LOCALLY (YET TO CLOSE)

COLLIERY	CURRENT MANPOWER	M/P CHANGE YEAR TO DATE	
GLASSHOUGHTON	419	-142	Closes in March 1986
LEDSTON LUCK	440	-1	Closes in 1986/7
FRYSTON	881	-96	NUM accepted closure 29:11:85
EMLEY MOOR	134	-77	Closes end December 1985
WHITWICK/ SOUTH LEICESTER	782	-186	Closes by July 1986
TOTAL 5	2656	-502	

NATIONAL APPEALS REJECTED AND REFERRED TO INDEPENDENT REVIEW BODY

	CURRENT MANPOWER	M/P CHANGE IN YEAR TO DATE	DATE OF APPEAL MEETING	DATE OF BOARD REJECTION OF APPEAL	REQUEST FOR REFERENCE TO I.R.B.
BATES	919	-505	11:9:85	18:10:85	NUM 21:10:85 / NACODS 25:10:85
HORDEN	877	-360	10:9:85	18:10:85	NUM 21:10:85 / NACODS 25:10:85 / BACM 30:10:85
TOTAL 2	1796	-865			

NATIONAL APPEAL MEETINGS HELD - AWAITING BOARD DECISION

	CURRENT MANPOWER	M/P CHANGE IN YEAR TO DATE	DATE OF MEETING
DARFIELD MAIN	505	-135	7:11:85
TILMANSTONE	503	-300	5:11:85
TOTAL 2	1008	-435	

NATIONAL APPEAL MEETINGS REQUESTED - YET TO BE HELD

	CURRENT MANPOWER	M/P CHANGE IN YEAR TO DATE	DATE OF UNIONS APPEAL
POLKEMMET	54	-640	NACODS 7:6:85/NUM 31:10:85
BETTESHANGER	702	-302	BACM 11:11:85
TOTAL 2	756	-942	

OTHER CLOSURES ANNOUNCED

			COMMENT
KINSLEY	344	-76	Closure proposed at Reconvened Meeting 19:11:85 : NUM opposing, NACODS and BACM considering.
TOTAL 1	344	-76	

GRAND TOTAL - 33 -

~~SECRET~~ A

CLOSURES OF OTHER ACTIVITIES

WORKSHOPS

CLOSED TO DATE

	DATE OF CLOSURE	MANPOWER AT CLOSURE	CURRENT MANPOWER
BLACKWELL	26:07:85	48	-
WHITBURN	28:09:85	49	-
CARCROFT	28:09:85	104	-
BIRDWELL	28:09:85	3	-
TONDU	28:09:85	61	-
KIRKLESS	31:10:85	23	23
ELSECAR	30:11:85	16	16
TOTAL 7		304	39

STORES

CLOSED TO DATE NIL

CLOSURES ANNOUNCED

	CURRENT MANPOWER	M/P CHANGE YEAR TO DATE	DATE ANNOUNCED	EXPECTED CLOSURE DATE	
CARCROFT	29	-3	8:8:85	end '85	All men have been interviewed for redundancy/transfer. Area Union officials wish to oppose the closure.
TOTAL 1	29	-3			

COAL PRODUCTS

CLOSED TO DATE

	DATE OF CLOSURE	MANPOWER AT CLOSURE
MANVERS REFINERY	12:7:85	20
HAWTHORN COKING WORKS	*	75
CAERPHILLY TAR PLANT	29:11:85	57
TOTAL 3		152

* Operations have ceased (Gas switched off 7:10:85) but screens are being maintained. Manpower will be further reduced to 30 in the near future (the level required for the screening/stocking operations - current manpower is 43).

CLOSURE AGREED LOCALLY

	CURRENT MANPOWER	M/P CHANGE YEAR TO DATE	
DERWENTHAUGH	218	-56	Expected to close end December 1985
LAMBTON	222	-29	Expected to close end January 1986
TOTAL 2	440	-85	

~~SECRET~~

COLLIERIES		CURRENT MANPOWER	M/P CHANGE YEAR TO DATE	OTHER ACTION TAKEN/ BEING TAKEN/ PROPOSED
(i) MERGERS	ALREADY MERGED : 4			
	DONISTHORPE/MEASHAM	1163	-141	Merged with effect from 31/3/85. No effect on output.
	OAKDALE/CELYNEN NORTH	1402	62	Merged with effect from 31/3/85. No effect on output. Unions have now agreed to the closure of the Celynen North surface.
	BLAENSERCHAN/SIX BELLS	766	-67	Merged with effect from 28/8/85. There will be some redundancy when the Blaenserchan surface is phased out, but there will be no effect on output.
	BULLCLIFFE WOOD/DENBY GR.	516	-197	Merged with effect from 2/9/85. There will be a net output reduction of some Some 77,000 tonnes
	AGREED FOR MERGER : 3			
	BARONY/KILLOCH	1693	-636	Unions have agreed to the merger of the two collieries with coal winding being concentrated at Killoch. Will take 18 months to complete. Combined manpower to be reduced to some 1200.
	BABBINGTON/HUCKNALL	1692	100	Merger agreed with Unions - Collieries will have one manager w.e.f. 1/1/86 but all men will not go down Hucknall shaft until end March 1986 - there will be no effect on output.
	MARDY/TOWER	1134	-221	Work has began on the underground link with Tower and when completed surface facilities will be withdrawn at Mardy with Union agreement. There will be no effect on output but manpower will be further reduced by about 40.
	NOTE : The merger of Woolley/North Gawber has also been agreed locally (see below)			
	PROPOSED FOR MERGER : 1			
	MANVERS/WATH/KILNHURST	1762	-393	Merger under single management control w.e.f. 1:1:86 proposed at GRCM 29:10:85. Reconvened Meeting being arranged for early December. There will be no effect on output in short term. Manpower will be reduced to about 1600.
	NOTE : The merger of Goldthorpe with Hickleton has also been proposed - details of the action so far taken at these collieries is already included in this table.			
(ii) PARTIAL CLOSURES	ALREADY CARRIED OUT : 1			
	GOLDTHORPE/HIGHGATE	610	-86	Highgate section closed at end 1984/5, reducing output by some 70,000 tonnes. Goldthorpe to be merged with Hickleton w.e.f. 1:1:86 for management purposes Unions have agreed in principle.
	PROPOSED : 4			
	* HAWTHORN COMPLEX (Eppleton/Murton/Hawthorn)	2307	-525	Area Director has announced that Complex is to be worked as one unit (Murton) which will involve the transfer of Eppleton underground men to Murton and the closure of the Eppleton surface. Overall manpower will be reduced by 400. NUM have appealed (13/9/85) Appeal Meeting was arranged for 5/11/85; NUM declined to attend following Board refusal to allow Lodge Secretary of Murton to take part (having been dismissed from the Board's employment). The NUM have requested that the Board should consider their appeal and if rejected the matter will be referred to the I.R.B.
	HOUGHTON MAIN	1242	-223	Partial closure proposed at GCRM 16/5/85. Reconvened meeting held and pit discussed further at GCRM 1/11/85 when the Area Director undertook to monitor progress further before finally deciding on withdrawal from the Dunsil Seam. Would result in net output reduction of some 70,000 tonnes.
	* WOOLLEY	1314	-174	Closure of Woolley upper measures has been agreed by BACM. NACODS have appealed (2/9/85) together with the NUM (30/10/85). Partial closure will result in output reduction of 321,000 tonnes. Merger of North Gawber with Woolley has also been agreed by BACMand NACODS. NUM have withdrawn their appeal locally. Merger with Woolley will result in output reduction of some 165,000 tonnes. Manpower required at merged unit is some 770.
	NORTH GAWBER	543	-163	

* DENOTES SUBJECT TO APPEAL

(iii) OTHER ACTION	TOTAL : 11	CURRENT MANPOWER	M/P CHANGE YEAR TO DATE	
	POLMAISE	137	-98	Unions have agreed to Polmaise being linked to Longannet and becoming a satelite shaft. Manpower to be reduced to 110.
	FRANCES	44	-465	40 men being retained at the pit to maintain access. 1983/4 output was 352,000 tonnes.
	ASKERN	792	-474	Two faces in the Warren House Seam have been closed involving an output reduction of some 170,000 tonnes.
	BENTLEY	880	-142	Workings in the Barnsley Seam have been concentrated - no change in output.
	BRODSWORTH	1140	-530	Barnsley and Dunsil Seams have been closed and the Newhill Seam will not now be worked, resulting in an output reduction of some 60,000 tonnes.A further face is to be stopped, reducing manpower to 1030.
	FRICKLEY	1294	-441	Barnsley Seam closed and Dunsil Seam will close when the last face finishes (about December 1985)resulting in an output reduction of some 60,000 tonnes.
	HATFIELD	1068	-[illegible]	Barnsley Seam closed but other developments mean that there is an output reduction of only 10,000 tonnes.
	HICKLETON	208	-141	Colliery now working on a "development-only" basis . 1983/4 output was 127,000 tonnes. Only one drivage to be operated. Manpower will be reduced to 100. Pit will be merged with Goldthorpe w.e.f. 1/1/86 for management purposes. The Unions have agreed in principle.
	DINNINGTON	675	-152	Unions have agreed limited production with concentration on development work - output will be reduced by some 110,000 tonnes.Manpower will be further reduced by some 200 to 475 by the end of March 1986. Coal Preparation Plant to be closed by end November with Union agreement.
	WARSOP	1134	-109	Manpower being reduced (with Union agreement) to about 1040.
	BIRCH COPPICE	543	-35	Manpower will be reduced to about 450 by end 1985/6 with a consequential reduction in output of some 30,000 tonnes in 1985/6
		24059	-5511	
WORKSHOPS				
	MOUNTAIN ASH	20	-41	Rationalisation has now been completed.
COAL PRODUCTS				
	MONKTON	103	-175	The works is not currently operating. Unions advised (18.10.85) production to be resumed as soon as technically feasible (December).
	NANTGARW	204	-48	Plant now being operated on a two-shift system(on four of the current five batteries). Manpower has been reduced to the required level.
	CWM COMPLEX (COKE WORKS AND POWER STATION)	288	-46	Plant will be operated on a two battery /two shift system in January 1986. Power Station is being gradually phased out.
	ABERAMAN PHURNACITE	753	-4	Unions have accepted that No.5 battery will cease to operate w.e.f. 23:11:85 (although the battery will be kept hot).There will be a manpower reduction of about 100 (to some 650) by end December 1985 (largely via redundancy).
		1348	-273	

CONFIDENTIAL

Any views on this?

FROM: P C DIGGLE
DATE: 30 April 1986

CR 1/5

1. MR ROBSON
2. CHIEF SECRETARY

cc Chancellor
Financial Secretary
Sir P Middleton
Mr F E R Butler
Mr Monck
Mr Moore

Yes: but discuss @ PRAYERS.

THE COAL BILL

This submission recommends that you reject Mr Walker's proposals for the content of next session's Coal Bill (his letter of 18 April). You should instead stimulate a collective debate on the fundamental issues facing the coal industry, and float some radical approaches.

The Bill

2. The Coal Industry Bill was given a firm place in the 1986-87 programme since the existing grant regime for the NCB expires at the end of this financial year. It was supposed to be a short (10 clauses) financial Bill. OL agreed its inclusion without discussion. We accepted it as part of the programme without commitment on its content. We took care to reinforce this message in writing at official level.

3. So far there has been little discussion of content. In negotiation over the 1986-87 Redundant Mineworkers Payments Scheme (RMPS), you got Mr Walker to agree to end Government finance for miners' redundancies at the end of this year. You also got him to leave open the question of financing responsibility for grant commitments accrued so far.

4. So discussions on the content of the Bill can start with more or less a clean sheet.

Mr Walker's proposal

5. The new grant regime Mr Walker offers is no more than an interim arrangement. In essentials, it differs insignificantly from the present rather complex range of grants:

(a) Future redundancies and pit closures would get grant under a relatively simple scheme with a single rate of grant which could vary year by year. The coverage would in fact be slightly wider than the existing scheme. The only real advantage is that this new comprehensive grant could be cash limited, whereas RMPS and social grants at present are not;

(b) Liabilities for redundancies and pit closures up to the end of this financial year would continue to be met by the Government;

(c) There would be reserve powers for deficit grant. It is hard to see how the temptation to use these could realistically be resisted.

6. This would certainly be better than the existing arrangements:

(i) It would be somewhat less complex;

(ii) The scale of support for new closure schemes could be progressively wound down, and perhaps responsibility for some existing financial responsibilities could be passed to the NCB;

(iii) RMPS would be cash limited. This might be an expensive minor victory in that it might also limit the Board's willingness to encourage redundancies.

7. These marginal advantages are not sufficient to outweight the serious flaws in these proposals:

(i) There is no incentive to break the deep established reliance on grant. A normal industry should bear its own redundancy costs, assessing them as an investment against future profitability;

(ii) The proposals are not rooted in a corporate plan. The NCB is still vacillating. It failed to produce a corporate plan in the relatively stable energy market in the eight months following the end of the strike last year. And in the five months since the oil price collapsed it has made no serious attempt to chart out the way ahead, still less to set about implementing it. By contrast private sector oil companies exposed to commercial pressures are already adjusting their investment plans and capacity requirements;

(iii) There is no progress on the main strategic aims for the coal industry (see below).

8. We therefore think you should reject Mr Walker's proposals. There is no point in arguing about the finer points of a completely unacceptable scheme.

Strategy

9. What we need instead is a good hard look at the coal industry's future. For this we need the long awaited business plan.

10. We think that the objectives should remain as stated in the Chancellor's minute to the Prime Minister of 2 September (copy attached). Discussion of that was delayed pending the appointment of a new corporate team at NCB. That is now virtually in place. So there is no reason for further delay.

11. In essence, we believe the three main aims should be:

(a) A robust financial discipline as near as possible to the commercial pressures of the market place. There is no reason why the NCB should be feather-bedded forever;

(b) Removal of the NCB's monopoly over coal extraction, with DEn becoming the licensing authority;

X (c) Powers to privatise the NCB's assets piecemeal, starting with the open cast sector but with scope for worker or management buy outs of individual pits too.

12. Taken together, these three measures would force a more realistic, commercial approach to the Board's deep mined output. It is important to remember that, so long as oil continues cheap, the CEGB could manage without <u>any</u> NCB deep mined coal since its fossil-fired power stations could be supplied by a combination of open cast, imports or oil substitution.

<u>Tactics</u>

13. The broad outline of this solution is obvious enough. But a forward business plan for the next few years is needed to set it in context. In the end it may make sense to adopt some features of Mr Walker's proposals; but giving ground now would enable him to further to procrastinate about producing the business plan. It is now well over due. There has been no serious in-depth discussion of strategy since the strike ended.

14. There seems little point in trying to persuade Mr Walker of the need for a more radical approach. The only way this could be achieved is by wider discussion including the Prime Minister. The Chancellor's minute of 2 September could be used as the basis for a Treasury paper.

<u>Recommendation</u>

15. We therefore recommend that you should:

(i) Reject Mr Walker's approach;

(ii) Urge a more fundamental reappraisal of the NCB's policy requirements;

(iii) Suggest the main features of an appropriate medium term strategy (end investing, privatising open cast and imposing a rigorous financial regime);

(iv) Insist upon a soundly based corporate plan with costed and evaluated strategic options to assist (ii);

(v) Propose that this discussion should take place collectively.

16. A draft in this sense is attached.

N. Lawrence

pp P C DIGGLE

1182/018

DRAFT LETTER TO:

The Rt Hon Peter Walker MBE MP
Secretary of State for Energy
Department of Energy
Thames House South
Millbank
LONDON SW1P 4QJ

1986 COAL INDUSTRY BILL

Thank you for ~~sending me a copy of~~ your letter of 18 April addressed to Nigel Lawson.

2. Your proposals basically amount to an extension of the existing arrangements for providing grants to the NCB. In my view we need to consider a Bill that goes a good deal further than this.

3. Our stance on the coal strike won widespread support. It is important, in both political and economic terms, to demonstrate that we are using our success in the strike to put the coal industry on a sensible footing and to stop the drain on the taxpayers.

4. I believe we need to put in place a rigorous financial regime for the NCB which breaks away from grants. The NCB needs to make a proper return on its deep mined activities. It needs to bear its own redundancy and restructuring costs just like any private sector company.

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4. I believe we need to put in place a rigorous financial regime for the NCB which breaks away from grants. The NCB needs to make a proper return on its deep mined activities. It needs to bear its own redundancy and restructuring costs just like any private sector company.

5. Beyond this we should end the NCB dominance over the coal industry. Coal extraction is not a natural monopoly. We need to open the way to much greater private sector activity in this area. To this end, the Bill should end the vesting of mineral rights in the NCB and the NCB's monopoly over coal extraction. The exploitation of coal should operate through a licensing system like that run by your department for oil and gas.

6. We should also give the NCB the powers to set up and sell subsidiaries. The Board's open cast activities are an obvious candidates for privatisation and, in the next Parliament, this power would open the way to the sale of individual pits.

7. I would favour an early discussion of the options ~~at~~ we ~~new~~ now face. To enable such a discussion to take place on a sensible basis, we ought to have a full corporate plan from the NCB examining the options facing the industry taking account of the uncertainties in the energy market. It is now over a year since the end of the strike and, while often promised, a Corporate Plan has yet to appear.

8. I am copying this letter to the Prime Minister, Willie Whitelaw, other members of E(A), John Wakeham ~~the Lord Provident, the Chief Whip~~ and to Sir Robert Armstrong.

JOHN MACGREGOR

Too much discussion. ~~[illegible]~~ Non-NCB topics [on] the agenda. But McG still keen that on key financial data to [illegible] of the RMPS. Other views noted below & on page 3.

CONFIDENTIAL

CHANCELLOR OF EXCHEQUER

FROM: MR S A ROBSON
DATE: 2 September 1986

cc Mr Monck
Mr Moore

SIR IAN MACGREGOR

1. This is a brief for your dinner tonight.

2. The number of guests (see attached list), and their wide range of interests, mean that this will not be an occasion on which you will be able to discuss the NCB in detail with Sir Ian. It would, however, be useful to get his thoughts on some more general points.

A. Financial Target

3. Does he still consider it realistic to achieve break-even by 1987-88? Mr Haslam is arguing that the target ought to be put back a year to 1988-89. — That is now McG's view assuming oil price well below $15

B. NCB Investment

4. NCB investment ambitions continue to look excessive. Their IFR bid is £650 million for 1987-88 and £750 million for 1988-89 and 1989-90.

5. This figure needs to be seen against the NCB's replacement cost depreciation of £742 million in 1985-86. It means the NCB is looking to invent enought to maintain the size of its business. This is very odd for a business which is meant to be contracting. It suggests a good deal of waste. You might like to point out that in a tightly run company like Hanson Truste investment tends to run at 80-90% of replacement depreciation and, unlike the

NCB, Hanson Trust does not have excess capacity and is showing (some) organic growth.

6. Moving on from the level of investment to the utilisation of investment, you might also query whether the NCB is making best use of its capital. This is an issue which could be discussed at the dinner in the context of British industry generally.

7. As regards the NCB, the German coal industry get about twice as much coal per $ of investment. Part of the reason is that German mines are bigger. But, on top of this, the equipment is used much more intensively. Four or 5 shifts per day are common in Germany compared to a maximum of 3 shifts per day in the UK. This means the equipment is more fully utilised in Germany. In 1982 the percentage utilisation of face machinery in Germany was 56.7%; for the NCB it was 34.6%.

8. You might ask MacGregor why the NCB do not push for more intensive working along the German model (as well as cutting down to a smaller number of pits).

C. Pit Closure

9. The NCB are talking in terms of 16,000 redundancies in 1987-88, 10,000 in 1988-89 and about 4,000 in 1989-90 and later years. By 1990 manpower should be down around 100,000.

10. This is a considerable advance on the position in 1983 but does Sir Ian think it is enough? It is based on 90mt of deep mined capacity. Sir Ian said this was too much even before the fall in the oil price.

11. You might ask why the NCB is not seeking a bigger (and faster) run down. It would be useful to know what Sir Ian sees as the main constraint - Mr Walker, the independent review body or NCB management?

D. Attitudes

12. It would also help to know whether Sir Ian considers the change in attitudes he has brought about is deeply and securely rooted. Has NCB management really changed from a cosy socialist collective to a market driven organisation? How much confidence has he that Haslam will secure the ground already won and push on forwards?

13. You may also like his views on the UDM's position. Is it now well established? How great is the risk of drift back of men to the NUM? It there anything that can be done to help the UDM advance?

UDM unlikely to advance, but solid where it is. Scargill has no hope of getting the miners out again: likely to frustrate future necessary restructuring – eg stopping nuclear power programme.

SAR

S A ROBSON

Mr Moore
Mr Robson

PRIVATE DINNER PARTY to be held at 39 Pont Street, London S W 1

Tuesday, 2 September 1986: 7.30 for 8.00pm : Informal

Hosts

Sir Ian MacGregor	Chairman, British Coal (until 31 8 86) & Limited Partner, Lazard Freres & Co
Mr Peter Grant	Deputy Chairman Lazard Bros & Co Ltd

Guests

Rt Hon Nigel Lawson MP	Chancellor of the Exchequer
Lord King of Wartnaby	Chairman, British Airways, & Chairman, Babcock Intern'l
Sir Campbell Adamson	Chairman, Abbey National Bldg Socy & Non-Executive Director, Lazard Bros & Co Ltd
Mr Donald Chilvers	Partner Coopers & Lybrand
Mr Eric Parker	Group Chief Executive Trafalgar House plc
Mr Duncan Penrose	Assistant Director Lazard Bros & Co Ltd
Mr Richard Davies	Director Lazard Bros & Co Ltd
(Joining later for coffee) Mr Ronald Grierson	Vice-Chairman General Electric Co plc

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Telephone: 588 2721

21 Moorfields
London EC2P 2HT

From: Mr. Peter J. Grant

Rt.Hon. Nigel Lawson MP
Chancellor of the Exchequer
11 Downing Street
London SW1

29 August 1986

Dear Nigel,

DINNER PARTY, TUESDAY, 2 SEPTEMBER

I refer to Sir Ian MacGregor's letter of 28 August enclosing guest list for the above dinner.

I wish to advise you that an additional guest has been invited - Sir Neville Bowman-Shaw, Chairman of Lancer Boss Group.

I look forward to seeing you on Tuesday.

Yours sincerely,

Peter

1 Tony OK
2 PWO

FROM: CATHY RYDING
DATE: 3 September 1986

MR ROBSON

cc Mr Monck
Mr Moore

SIR IAN MACGREGOR

The Chancellor was grateful for your minute of 2 September.

2. The Chancellor has commented that too many were present at the dinner. Non-NCB matters topped the agenda, but he reports that Sir Ian MacGregor was still keen that an early terminal date is put to the RMPS.

3. On your paragraph 3 that Mr Haslam is arguing that the target for break-even should be put back a year to 1988-89, the Chancellor reports that this is now Sir Ian's view - assuming an oil price not below $15.

4. On your paragraph 13, the Chancellor has commented that the UDM is unlikely to advance, but is solid where it is. Mr Scargill has no hope of getting the miners out again in the forseeable future: he is likely therefore to become increasingly involved elsewhere - for example stopping the nuclear power programme.

CR

CATHY RYDING

SECRET ~~SECRET~~ AR

COPY NO 2 OF 11

CH/EXCHEQUER
REC. 05 SEP 1986
ACTION: MR ROBSON
COPIES TO: CST FST, SIR P MIDDLETON, SIR T BURNS, MR F E R BUTLER, MR MONCK, MR MOORE, MR CROPPER

√ 5/9

C/ might like to be aware
CR 5/9

SECRETARY OF STATE FOR ENERGY
THAMES HOUSE SOUTH
MILLBANK LONDON SW1P 4QJ
01 211 6402

Mark Addison Esq
10 Downing Street
LONDON
SW1

5 September 1986

I am, at 1st sight, concerned @ X, & wd welcome Mr R's views. I do not believe that Y is an accurate description: what wd be dangerous is the fact that Haslam is to stir ... Scargill ...

Dear Mark,

BRITISH COAL: PRESS CONFERENCE

I am writing to let you know that the new Chairman of British Coal, Sir Robert Haslam, will be holding a press conference on Monday 8 September, at which he intends to make a number of important announcements. As these are likely to provoke immediate union and media reaction, some of which could well be misleading, the Secretary of State has asked me to write to you and other colleagues with the facts and the background.

Y Sir Robert believes that there are two major issues underlying the considerable discontent in the coalfields: failure to pay the 1985 increase to all UDM members and to NUM members, especially those who worked for all or part of the strike; and dismissals. On both these Sir Robert believes that some action must now be taken in an effort to resolve current industrial relations problems.

British Coal made a pay offer, of £5.50 on basic rates plus an additional shift allowance, to the UDM towards the end of last year. This offer was accepted by the UDM in November and immediately paid with effect from 1 November to all mineworkers at pits where UDM members were the majority. The same pay offer was made to the NUM but was conditional on their acceptance that strikers would have to make contributions to the pension fund if their period on strike was to count towards their pensions. Although the NUM made clear they could accept the pay offer, they were not prepared to accept the pension condition. The offer was eventually withdrawn. The UDM leaders had meanwhile given their agreement to the principle that additional contributions should be made to the pension fund to cover strike periods.

PS How Scargill's pressure ...

Sir Robert now intends to impose on the NUM the wage increase as offered, to be paid with effect from 1 September 1986. For those NUM members who worked for all or any part of the strike, this increase would be back-dated, pro rata, to 1 November 1985. The

SECRETARY OF STATE FOR ENERGY

money not used for retrospective payments, where these have been withheld, will be set aside by British Coal pending resolution in the courts of a dispute over the meaning of the Pension Scheme rules in relation to strikes, so reaffirming British Coal's point of principle in relation to pension contributions. For those members of the UDM not yet receiving the wage increase, it will be awarded with full retrospection to 1 November 1985 in all cases, in recognition of the fact that UDM leaders had accepted the point of principle on the pension issue. This will be the grounds for defending this apparent discrimination in favour of the UDM.

On the issue of reinstatement, Sir Robert plans to announce a final internal review by British Coal at national level of certain outstanding cases. He will make it clear that there are certain categories of offence, including all those involving violence or wilful damage, which will not be reconsidered; also excluded will be cases where men have already accepted payment in lieu of reinstatement. Those mainly concerned, and the numbers are relatively small, will be men who chose not to go to Industrial Tribunals or who failed to do so within the prescribed timescale.

X Both the Secretary of State and the Chairman are well aware of the risk that attempts may be made to portray these announcements as a sign of some softening on the part of British Coal top management. The Chairman will make clear that this is not the case. In particular he will stress that there will be no backdating of the pay award for NUM members on strike throughout the dispute and that British Coal maintains its position of principle on the Pension Scheme. He will also make clear that future wage offers will be based primarily on incentive schemes. Moreover the press conference will begin with a scene-setting which will stress the problems that still face the industry and the continued need to cut costs if it is to succeed in the market place. The Chairman may also give some indication of the need for further reductions in high-cost capacity: as the
Prime Minister and the Secretary of State for Scotland are aware, specific proposals will begin to emerge later next week.

I am copying this letter to Alex Allan (Treasury), Leigh Lewis (Employment), Robert Gordon (Scottish Office), Colin Williams (Welsh Office), Andrew Lamsley in Norman Tebbit's Office and Joan Naughton in the Lord President's Office.

Yours,

Stephen

S R SKLAROFF
Private Secretary

~~SECRET~~ 8/12

1. ~~Alex~~
2 Tony O/R
3 PWD

FROM: CATHY RYDING
DATE: 8 SEPTEMBER 1986

MR ROBSON

cc Chief Secretary
Financial Secretary
Sir P Middleton
Sir T Burns
Mr F E R Butler
Mr Monck
Mr Moore
Mr Cropper

BRITISH COAL: PRESS CONFERENCE

The Chancellor has seen Mr Sklaroff's letter to Mr Addison of 5 September.

2. The Chancellor was at first sight concerned at the comment in the second paragraph that there is considerable discontent in the coalfields, and would welcome your views.

3. The Chancellor does not believe that the comment in the penultimate paragraph that both the Secretary of State and the Chairman are well aware of the risk that attempts may be made to portray these announcements as a sign of some softening on the part of British Coal top management is an accurate description at all: what would be dangerous is the feeling that Sir Robert Haslam is a softy and the Government is running scared.

4. The Chancellor wonders how Mr Scargill would react to this move if it was made.

C.R

CATHY RYDING

~~SECRET~~

FROM : S A ROBSON
DATE : 8 SEPTEMBER 1986

CHANCELLOR OF EXCHEQUER

c.c. Chief Secretary
Financial Secretary
Sir P Middleton
Sir T Burns
Mr F E R Butler
Mr Monck
Mr Moore
Mr Cropper

C/ You asked a number of questions on the attached letter from Walker's PS. Letter to issue?

CR 8/9

No: given the satisfactory press Haslam has got for this, no need.

BRITISH COAL : PRESS CONFERENCE

Mr Walker's PS sent a letter to No 10 on 5 September. This is a pretty crude bounce as it forewarns of the content of a press conference Haslam is giving today.

2. Essentially Haslam intends to announce some sweeteners on the implementation of the 1985 pay awards and on the review of dismissed miners. The substance of these issues is not important. The key question is whether Haslam is striking the right stance and the right tone for his first public appearance as chairman.

3. The background is as follows. Haslam has been going round the coalfields "listening" to the mood. He told Mr Hunt that there was at the grass roots a restlessness. As you will know there is an overtime ban in South Wales (which is about a month old) and some rumblings of similar action in Durham and Yorkshire.

4. The source of unease is a combination of facotors :

(i) miners have still to get used to British Coal managers taking decisions. This is not the style of life they are used to;

(ii) the non-payment of the 1985 pay increase;

(iii) the non-reinstatement of sacked miners.

SECRET

~~SECRET~~ AK

The NUM are having no difficulty in keeping this running;

(iv) continued closures.

5. The decision to have an overtime ban in Wales was generally unexpected. The non-payment of the 1985 pay increase seemed to be a particular irritant in that case.

6. More generally Scargill is seeking to build again. He is not being successful. He is isolated in the NUM. He is not getting any encouragement from any coal field on support for a strike.

7. The possibility of the Welsh overtime ban spreading cannot, in Department of Employment's view, be ruled out. But they continue to think we are a "long, long way" from a major confrontation.

8. Against this background it is not easy to say whether Haslam's concessions were well judged. They may be relevant but it is unfortunate he gave them without getting anything in return. The NUM may see this as softness. In any event it looks as though Haslam is signalling a readiness to be a "healer" or a "compromiser".

9. In the end the main aim must remain to get capacity in line with market prospects. Given this uncertain start by Haslam, it would be useful to rub home this message. As you know, British Coal's IFR bid is based on a deep mined capacity of 90 million tonnes. Sir Ian MacGregor said this was too high even before the fall in oil prices.

9. A draft is attached. It is designed to avoid cutting across the Chief Secretary's IFR disucssion with Mr Walker.

SAR

S A ROBSON

DRAFT LETTER FROM CHANCELLOR TO SECRETARY OF STATE FOR ENERGY

BRITISH COAL : PRESS CONFERENCE

I have seen a copy of your private secretary's letter of 5 September.

2. It is unfortunate that we were not given longer notice of the line ~~Sir Robert~~ BOS Haslam was intending to take. I have misgivings about it. ~~Sir Robert~~ He appears to be making concessions without extracting anything in return. Miners and their union leaders may well draw some unfortunate conclusions about British Coal's new management.

3. ~~Sir Robert~~ Haslam should be left in no doubt that the key objective remains that of reducing British Coal's capacity to bring it into line with the prospects for profitable sales. It is far from clear that the level of deep mined capacity assumed in British Coal's current public expenditure proposals is consistent with this objective. John MacGregor will wish to discuss this with you in your bilateral meeting later this month.

4. I am copying to the Prime Minister, David Young, Malcolm Rifkind, Nicholas Edwards, Norman Tebbit and Willie Whitelaw.

N L

1 ~~Alex~~
2 PUP

FROM: CATHY RYDING
DATE: 9 SEPTEMBER 1986

MR ROBSON

cc Chief Secretary
Financial Secretary
Sir P Middleton
Sir T Burns
Mr F E R Butler
Mr Monck
Mr Moore
Mr Cropper

BRITISH COAL: PRESS CONFERENCE

The Chancellor was grateful for your minute of 8 September.

2. The Chancellor thinks that given the satisfactory press Haslam has received for this, there is no need for him to write to the Secretary of State for Energy.

CR

CATHY RYDING

AK

COPY NO 2 OF 8

How much wd it cost to increase stocks a little more by Nov. 1988? Say to 30-33 m tns

PRIME MINISTER

COAL STOCKS AT CEGB POWER STATIONS

Stocks at CEGB power stations on 26 October were 26.8 mt and had reached 27 mt by 2 November, thus meeting our target. Given normal weather conditions, stocks should continue to rise for the next few weeks further consolidating the position. The present level of stocks means that we now have one year's endurance with no coal deliveries at all; endurance would be extended to around the summer of 1989 on the assumption that 400 kt of coal a week could be delivered from UDM areas.

British Coal and the CEGB have agreed the necessary coal supply arrangements for the winter with a view to providing a stock of 22 mt at the end of March 1987. For future years it should the be possible to cycle around these figures of 27 mt in October and 22 mt at the end of March to provide us with an adequate level of endurance throughout the year.

I am copying this minute to Nigel Lawson, Malcolm Rifkind and Sir Robert Armstrong.

CH/EXCHEQUER	
REC.	12 NOV 1986
ACTION	Mr M Williams
COPIES TO	FST, Mr FER Butler, Mr Monck, Mr Moore, Mrs Brown

Secretary of State for Energy
12 November 1986

pwp

10 DOWNING STREET
LONDON SW1A 2AA

From the Private Secretary

14 November 1986

CH/EXCHEQUER
REC. 14 NOV 1986 14/11
ACTION M Williams
COPIES TO FST, FER Butler, Mr Monck, Mr Moore, Mrs Brown

COAL STOCKS AT CEGB POWER STATIONS

already in

The Prime Minister was grateful for your Secretary of State's minute of 12 November reporting the position on coal stocks at CEGB power stations.

I am sending a copy of this letter to the Private Secretaries to the Chancellor of the Exchequer, the Secretary of State for Scotland and Sir Robert Armstrong.

(DAVID NORGROVE)

Geoff Dart, Esq.,
Department of Energy

RC2.85

~~SECRET~~ NC

Tony O11
b/f with response

FROM: CATHY RYDING

DATE: 17 November 1986

MR M WILLIAMS

cc Financial Secretary
Mr F E R Butler
Mr Monck
Mr Moore
Mrs Brown

COAL STOCKS AT CEGB POWER STATIONS

The Chancellor has seen the Secretary of State for Energy's minute to the Prime Minister of 12 November.

2. The Chancellor would be grateful to know how much it would cost to increase stocks a little more by November 1988 - say to 30-33 million tons.

CR

CATHY RYDING

SECRET

B/F with response to my minute of ~~today~~. or 19/11
CR 17/11

FROM: P C DIGGLE
DATE: 17 November 1986

17.11

1 MR M WILLIAMS

2 CHANCELLOR

cc: Chief Secretary ← NB for circ list
FST
Mr F E R Butler
Mr Monck
Mr Moore
Mr Scholar

COAL STOCKS AT CEGB POWER STATIONS

Mr Walker's minute of 12 November to the Prime Minister is intended to reassure her that coal stocks are adequate to withstand the risk of strike over the coming winter. You need not join in the correspondence.

2. During the summer the Prime Minister expressed some concern, in correspondence which we did not see, that the intended stocks target (22 million tonnes) at CEGB power stations was not reached last March. The short fall was involuntary. It happened because February and March 1986 were extremely cold. This not only stimulated electricity consumption but also made it difficult physically to shift coal to power stations, for example because of difficulties with the merry-go-round trains.

3. The short fall was not large: about 2MT. Endurance was not seriously at risk.

4. Nevertheless CEGB have been quietly encouraged to get their stocks back on track. They have now managed to achieve 27MT by the beginning of the winter. With normal electricity consumption stocks would fall to 22MT by the end of this financial year, sufficient to give endurance of a good year against an all out strike.

5. This has been achieved <u>without</u> any additional cost to public expenditure by:

(a) burning extra oil during September - equivalent to about 1.5MT of coal;

(b) arranging for delivery of an extra 2MT of coal on deferred payment arrangements. This is costless to public expenditure since it was effectively drawn from British Coal's stocks;

(c) importing some additional Scottish electricity to cope with demand peaks during the summer.

6. In fact the endurance now available is rather better than the one year envisaged when the 27MT objective was established after the strike, because:

(i) the 2 GW interconnector with France is now available. This could deliver nearly 8MTCE if it ran at fullcapacity for a year;

(ii) the three AGRs at Dungeness, Hartlepool and Heysham 1 are all now close to fully commissioned and capable of providing perhaps 9MTCE in a full year. During the strike their output amounted to only about 2MTCE;

(iii) the UDM is now better funded and might well be able to prevent total cessation of coal deliveries during a strike.

7. You will recall the Prime Minister's interest last year in boosting coal stocks even further. This would obviously be costly. It therefore seems desirable to play this issue in a low key way so far as is possible. I therefore suggest that you avoid commenting on the correspondence unless the Prime Minister intervenes to suggest higher stocks. You might then write drawing attention to the points in para 6 .

P C DIGGLE

SECRET

FROM: P C DIGGLE
DATE: 20 November 1986

1 MR M WILLIAMS

2 CHANCELLOR

cc: Chief Secretary
Financial Secretary
Mr F E R Butler
Mr Monck
Mr Moore
Mrs Brown

COAL STOCKS AT CEGB POWER STATIONS

You asked how much it would cost to raise CEGB's coal stocks over the next couple of years.

2. Assuming that the ESI would not regard the cost of extra purchases of coal as a normal business expense, the entire cost would feed through to EFLs in 1987-88 and/or 1988-89. Assuming also (in line with the price arrangement between CEGB and British Coal) that the additional coal for stock would be supplied at first tranche prices, ie some £30 a tonne, the necessary addition(s) to ESI's EFLs for 1987-88 and 1988-89 would be £90-£180m. It if were possible to persuade the ESI to reflect this extra cost in prices, it would add 1-2%. This would not be an onerous burden given the intention not to alter nominal prices next spring.

3. On top of the probable cost of restocking to the ESI, there would also be the effect on the coal industry. This would almost certainly be adverse. Since British Coal's stocks are historically low, it would probably be necessary to increase production, with some inevitable slowdown in progress toward improved efficiency and productivity. This effect would obviously be limited if the stock growth were phased over two years; but it would still run counter to all the other financial pressures which have been engineered to force the coal industry to improve efficiency and shut uneconomic pits.

4. Since British Coal's productivity targets are very demanding, it seems rather unlikely that coal production will exceed market demand as has happened in the past. However, if it did, it would obviously be logical to encourage a deal with CEGB to mop up the extra production. Better endurance

would be secured by this means even if the deal were on deferred payment terms, ie paid for only when burnt.

5. But for the moment we see no need to plan such contingencies. Stocks of 27MT at the beginning of this winter give us comparable endurance to the pre-overtime ban stocks carried by CEGB in 1983, as explained in my note of 17 November (below)

Pcdiggle

P C DIGGLE

RT4.66

~~SECRET~~ AK

P

FROM: A W KUCZYS

DATE: 21 November 1986

MRS DIGGLE

cc PS/Chief Secretary
PS/Financial Secretary
Mr F E R Butler
Mr Monck
Mr D J L Moore
Mrs Brown
Mr M Williams

COAL STOCKS AT CEGB POWER STATIONS

The Chancellor was grateful for your note of 20 November. (He had not seen your earlier note of 17 November when he asked the question in Cathy Ryding's note of the same date.)

2. He was not, of course, envisaging achieving higher power station stocks by increasing production, but either by running down pithead stocks on a deferred payment basis or by oilburn as and when it is economic to do so. (It may be true that British Coal's stocks are historically low, but why not historically lower still?) The Chancellor takes it from your notes that the cost of doing what he suggests would be small?

3. There is no need for any action now, but we would need to consider this at the first whiff of trouble.

AWK

A W KUCZYS

CH/EXCHEQUER

REC.	27 NOV 1986
ACTION	Mr M Williams
COPIES TO	FST, FER Butler, Mr Monck, Mr Moore, Mrs Brown

27/1

~~SECRET~~

Prime Minister

COAL STOCKS AT POWER STATIONS

I have seen Peter Walker's minute of 12 November.

Coal stocks at SSEB stations at 7 November were 1.84mt which exceeds the target level of 1.75mt for this time of year. Stocks will be run down to around 1.3mt by end March 1987. Given the substantial oil and nuclear generation capability within the Scottish system, the Scottish Boards regard the endurance of the Scottish system with no coal deliveries as virtually indefinite.

I am copying this to Peter Walker, Nigel Lawson and Sir Robert Armstrong.

MR

MALCOLM RIFKIND

HMP32909

STRICTLY ~~CONFIDENTIAL~~ AK

[Which 1st: coal or elec. generation? Competition & competition for both]

PS. I am allergic to the left to tip coal. How much economically recoverable coal @ present tests in British coal tips? NL

THE PRIVATISATION OF THE BRITISH COAL INDUSTRY

An Examination of the Case for Privatisation, the Choice of Methods, and Recommendations on the Preferred Method and Programme.

A useful paper.

Key points wh. emerge are

(i) The ~~[illegible]~~ close connection between coal production & electricity generation – which shd be privatised first?

(ii) In both cases, there are not – unlike electricity, gas & water transmission & distribution – natural monopolies: ~~[illegible]~~ privatisation must therefore focus on the creation of competition & the breaking up of the present monopoly arrangements.

1st December, 1986

(iii) The achievement of this, which may ~~[illegible]~~ be best achieved by selling the various coal and/or power station companies to corporate buyers. Shd take place over work share ownership.

(iv) With share ownership by contrast, as in water for the area elec boards.

(v) The National Grid would probably need to be owned jointly by the various ~~[illegible]~~ area elec boards/companies.

(vi) I am not convinced of the need for a Coal Commission. Is the case made, or the job [illegible] D.Bn.

NL.

THE PRIVATISATION OF THE BRITISH COAL INDUSTRY

CONTENTS

FOREWORD

Privatisation of the coal industry, if carried out responsibly, imaginatively, sympathetically and with the introduction of competition, could benefit customers, taxpayers, mine workers and, indeed, the nation as a whole.   The potential benefits include increased competition bringing lower energy costs, significant coal export opportunities, and hence the coal industry's best contribution to national employment prospects.

This paper examines the various ways in which firstly, liberalisation and secondly, privatisation of the coal industry could best be achieved.   The identification of the best methods is inseparable from the case for privatisation.

1. <u>WHY PRIVATISE THE COAL INDUSTRY?</u>

Now that the nation has successfully overcome the miners' strike the nationalised coal industry is in better shape than it has been for many years. British Coal has been radically changed by the closure of high cost collieries resulting in reduced losses and increased productivity. Given these major improvements, long held to be unachievable, it may reasonably be asked whether a good case still exists for coal privatisation. This is a reasonable question. It is the purpose of the first part of this report to demonstrate briefly, but comprehensively, the further <u>major</u> benefits which could be achieved by privatisation. The cumulative effect of these benefits would surpass the very welcome and significant improvements of the last eighteen months. Imaginatively presented they can offer a secure and profitable future for the coal industry.

Eleven main benefits have been identified.

(1) <u>Increased efficiency</u>

A privatised coal industry consisting of entrepreneurial mining companies would have a major incentive to make full use of equipment. It would also experiment with a variety of mining techniques which have proven successful in other countries.

British Coal is recognised as a world leader in the development of equipment and technology for the longwall system of underground extraction. Unfortunately the productivity obtained from similar equipment varies considerably between different regions of the country and the average is below international standards.

Increased competition and the free movement of technical and administrative personnel, aided by transferable pensions, are essential if the full productive potential of high cost capital equipment is to be realised.

The removal of avoidable inefficiency will make a significant contribution to reduced energy costs to the clear benefit of customers, taxpayers and the nation at large.

(2) **Monopoly breaking**

The reasonable case for public ownership or regulation usually relates to "natural" monopolies which, if privately owned, could exploit customers due to the lack of competitive forces. Coal is not a "natural" monopoly, but a naturally competitive industry extracting a variable product dispersed by nature. There is no economic reason why coal production in the United Kingdom should be in the hands of one or indeed few organisations. After privatisation, assuming that the industry is not privatised as a monolith, the inevitably resulting market pressures would guarantee the best and quickest responses to customers' needs. Even the total dedication of management in a huge monolithic industry is a poor substitute for the liberalising forces of a competitive market.

Management attitudes within British Coal have not been based upon commercial standards since the industry has not been run on a commercial basis for 40 years. When all suppliers of coal are in the same organisation, there is little incentive to make changes in any part of the industry if such changes will impact detrimentally upon the operations of another part of that industry.

With one coal company, and restricted imports, neither the management of that company (nor anyone else) has relevant performance standards against which to measure its acts and achievements even assuming there was sufficient incentive for maximum efficiency.

(3) **Reduction of costs**

Since the present coal mining organisation is state-owned commercial objectives have been largely subordinated to social and/or public service objectives, and there has been continual political interference in the industry. The production costs of coal in the United Kingdom have remained quite unnecessarily high and - despite a protected market - the industry has fairly easily extracted large subsidies from both the British taxpayer and electricity consumers. Unnecessarily high coal prices have resulted in unnecessarily high electricity prices, contributing significantly to the decline of the British manufacturing industry and to the rise in general unemployment. Without privatisation minimum costs cannot be achieved.

NB so

(4) Restoration of commercial direction

The large real oil and gas price increases over the last 14 years presented British Coal with an unparalleled opportunity to increase its market share. In fact, far from increasing its market share in these very favourable conditions, that share continued to decline. One of the greatest business opportunities since the end of World War II was entirely missed. There were two main reasons for this: on the supply side, British Coal lacked any compelling commercial imperative; on the demand side, customers (both the Electricity Boards and industry) were fearful of increasing their dependency upon British Coal because of the monopolistic positions of both British Coal and the National Union of Mineworkers, and the effective ban on more than token imports.

During the years since 1971, both Australian and South African coal production has risen by a factor of almost 3. In contrast, coal production in the protected United Kingdom market has fallen by around 20 per cent over the same period. Only privatisation can introduce full commercial attitudes to exploit the many neglected business opportunities.

(5) Enhanced security of supply

Security of coal supply would be greatly enhanced by the diversification of sources of supply and competition, including imports. There would be little likelihood of concerted action by foreign producers to use coal as a political weapon against

That's [illegible]

the United Kingdom given their wide geographical spread, their diverse political systems and the existing strong competition between them. Indeed, the United Kingdom could become an exporter of coal to Western Europe if production costs fall to the achievable minimum.

(6) <u>Return to free market</u>

After privatisation of the industry, no <u>economic</u> regulatory authority would be needed because prices would be set by competition within the coal industry, between indigenous coal and imports, and between coal and other fuels; and the Monopolies and Mergers Commission would exercise its traditional responsibilities. To confine competition merely to a national coal monopoly and three other fuels, two of which are also presently monopolies (gas and electricity) is to miss out the main opportunity for competition. The privatisation exercise requires careful and specialist handling since it would involve privatising British Coal in numerous self contained units. This would involve addressing a number of issues which have not had to be faced before. A range of specialist skills should be assembled which could help the Department of Energy to produce the most effective mechanism for privatisation. Once privatisation is complete there will need to be a new permanent Government entity to hold and allocate future coal reserves, with certain other residual responsibilities - see Section 3. below.

! natural monopolies (public utilities) Tho' not electricity <u>generation</u>, any more than gas production.)

? cf oil

(7) <u>Removal of subsidies</u>

The privatisation of the coal industry would remove most of the still very considerable subsidies paid by the taxpayer and electricity consumer, subsidies which would be generally unnecessary in a fully competitive industry.

(8) <u>Optimal reserve usage</u>

The privatisation of coal would promote optimal usage of the Nation's coal resources, that is long term profitability resulting from achieving the best balance between financial performance and systematic extraction of coal reserves.

Successful private mining companies would have to be responsive to market requirements in terms of coal quality and price. This could best be achieved by giving such companies the opportunity to construct mining units which covered one or all of the various sources of coal (underground, opencast and tip coal).

(9) <u>Improved employee benefits</u>

For any given level of output, while fewer people would be employed than before, they would enjoy much greater opportunities for increased pay, plus profit sharing. A diversified, competitive industry would have lower costs, higher productivity and enhanced security of supply. Market opportunities, both at home and abroad, should increase, and total production could rise. The result of this would be greater job security which would be both genuine and deserved since it would be based upon the enduring stability of efficiency rather than the illusion of security created by begrudged taxpayer subsidies and union militancy. In a privatised industry the workforce would benefit from the circumstances prevailing area by area. Growing efficiency would be rewarded as each colliery would have the incentives to realise its full potential.

(10) <u>Improved UK energy sector</u>

It is important to appreciate that maximum benefits from coal privatisation would ensue only if the entire United Kingdom energy sector were to be privatised, and in particular, electricity <u>generation</u>. To maintain electricity generation under single ownership would negate much of the benefit of coal privatisation. Of the strong rationale which justifies coal privatisation, much applies to privatising electricity generation, an industry which normally absorbs 70 per cent of the United Kingdom's coal production. Accordingly the benefits of privatising coal would be much enhanced if electricity generation were also to be privatised. Also, private sector companies would be much more likely to buy and pay better prices for coal mines and reserves if electricity privatisation were certain to follow.

(11) Opportunities for creativity

The coal industry is not only a "mature" industry, but one which for two generations has not been subject to commercial pressure. It is, therefore, a fertile area for imaginative entrepreneurial flair at all levels of workforce and management. British miners, given the right stimulus, incentive and opportunity, surely have a major contribution to make. Local management must be permitted to introduce systems and methods which are applicable to local conditions rather than be constrained by rigid single national procedures.

2. PRESENT STATE AND STRUCTURE OF THE INDUSTRY

Before turning to the case for and the methods of privatising the coal industry, the present state and structure of the industry needs to be described. It is important to appreciate that Britain has huge coal reserves which are widely held to be sufficient for several centuries. This contrasts with oil and gas reserves which are expected to be of much shorter duration.

British Coal Production

During the year ended March 1986 (the first year of "normal" operations since the strike) coal production from the deep mines sector was 87.8 million tonnes and that from opencast operations 14.1 million tonnes, a total of nearly 102 million tonnes.

What was the no. in 1978-79?

A. Deep Mining - despite radical reorganisation and the closure of many unprofitable collieries (the number of operating collieries has fallen from 200 in 1981/82 to 133 in 1985/86 and will fall further to 110 during the current year), the underground mining sector of British Coal continues to return operating losses. These "operating" losses totalled £171 million in 1985/86 (see British Coal latest report and accounts, and the appendix to this report), representing an average loss of

£1.95 per tonne of deep mined coal. Only two of the ten British Coal deep mining Areas, South Yorkshire and Nottinghamshire, were profitable; and losses ranged from £10.6 per tonne in the Scottish Area to £2.7 per tonne in the South Midlands Area.

Increases in productivity and improvements in financial performance with the "new management style" after the strike are evidence of what effect some external pressure can have on the industry. Even greater achievements should be realised after privatisation providing, of course, that the form of privatisation is well chosen - see Section 3 below.

B. Opencast Mining - whilst small in comparison with the underground mining sector, this sector is nevertheless highly profitable. Mining operations are carried out by private contractors, subject to highly competitive tendering, and in recent years the operating profits of the Opencast Executive of British Coal have been £211 million (1983/84), £142 million (1984/85) and £343 million (1985/86) - see British Coal annual report and accounts. The 1985/86 results represented an operating profit of £24.33 per tonne, by far the most profitable part of British Coal's activity, and likely to remain so. Accordingly it may well be desirable to increase the tonnage from this sector, subject to environmental considerations. This possibility deserves an early objective review.

C. Other British Coal Activities - these include coal processing into coke and smokeless fuel, distribution services, consultancy, etc. Over recent years, these activities broke even in 1983/84, but returned losses in 1984/85 and in 1985/86. British Coal's record in these activities is poor when compared with that of the private sector firms who are very active in this area. The recovery of coal from old colliery tips has been severely restrained by British Coal and yet coal tip coal can be as cheap as, or on occasions even cheaper than, opencast coal. As coal tip removal both creates jobs in areas where coal mining is no longer a major source of employment and improves the environment, this activity also deserves an objective early review.

How much is economically recoverable?

During the first six months of the current year British Coal reported an overall operating loss of £240 million after payment of interest charges, and the Chairman indicated a full-year loss "contained within £300 million".

Present Financial Structure

British Coal is supported by a variety of government grants. Moreover, it has an easier financial target to meet than most other nationalised industries; it is at present charged only with breaking even after interest payments and receipt of "social grants" from government (grants for premature pensions, pit closures, concessionary coal and to cover deficiencies in the mineworkers' pension scheme). In fact, even this target has not been achieved in recent years and the latest break-even target date (1987-88) set in the 1985 Coal Industry Act has already been put back to 1988-89 according to British Coal's Chairman.

British Coal and British Rail have by far the largest External Financing Limits (i.e. borrowings and grants from external sources) among the nationalised industries. Each has an EFL of over £700 million in 1987/88: the sum of the EFLs for all nationalised industries is only £690 million, including industries such as electricity supply which are net contributors to the Exchequer.

Direct government grants totalled £1,471 million during the year ended 31 March, 1986:-

Direct Government Support	(£ million)
Deficit Grants	392
Social Grants	450
Pension Scheme Contributions	63
Redundancy Payments Scheme	566
	1,471

The average workforce during the same period was 155,000 men and this government support represents a subsidy of £9,500 per man employed by British Coal (cf. the average wage of £10,100) representing currently 31% of British Coal's operating costs.

why? ? Social grants

Of these payments, the Deficit Grants and Redundancy Payments would cease upon privatisation; the other payments would probably continue in some measure.

In addition, the government provides loan finance and guarantees bank loans to British Coal:-

Loans	As at 31 March, 1986 (£ million)
Loans, under Coal Industry Act 1973	145
Other government loans	2,284
Government temporary advances	599
Bank loans (guaranteed by Treasury)	765
	3,793

Private Sector Production

An active, generally profitable, but highly constrained, private coal mining sector is at work in the United Kingdom, producing 1½ per cent of total national production from about 160 very small underground mines and 60 very small opencast sites.

The Coal Industry Nationalisation Act (1946) limits the size of private sector mines, and allows British Coal to control the number of private operations by requiring those operators to hold a licence issued by British Coal, to pay royalties to British Coal, and to accept selling prices imposed upon them by British Coal.

In other words, British Coal can decide just how much competition it will allow, and can nominate its competitors!

It acts both as "judge and jury" over the private sector - for example, the recent "joint understanding" negotiated between British Coal and the CEGB halved without any discussion the quota for the cheapest coal available in Britain as supplied by the private mining sector. This cosy deal between two large public sector monopolies reduced the market for this private sector coal from 3 to 1½ million tonnes per year. The national interest has been ill-served by this action. Such coal originates from privately-operated tiny underground mines, small opencast operations and small-scale working of British Coal discard tips. All of these - the fringe areas of the industry - produce profitable coal as the result of enterprising management.

Despite having the least economic reserves, the smallest production units, and no subsidies, this is a profitable sector of the industry. Its record alone indicates the major benefits obtainable only from efficient (diversified) privatisation.

Marketing

The CEGB is British Coal's largest customer, taking almost all of its coal requirement from British Coal. As a result of successive governments taking action to protect the coal industry, the CEGB has been prevented from diversifying its supplies, especially via the international market where imports for use in electricity generation have been reduced to token proportions. The latest "joint understanding" between British Coal and the CEGB, requires the CEGB to take 95 per cent of its coal requirements from British Coal (equivalent to around 70 million tonnes per annum), effectively stifling the private sector. Of this total tonnage, 50 million tonnes will be at a base price of £47 per tonne, 10 million will be at a lower price related to the cost of imported coal (£34), and another 10 million will be related to the current price of oil (£29.50per tonne of coal).

Given this comfortable market situation, plus protection from imports, British Coal has had no incentive to consider the export of coal in significant quantity since its protected costs of production have always been well above the prices of internationally traded coal, and there has been no compelling incentive to get them down. Yet with an efficient (i.e. diversified) form of privatisation, exports to Western Europe could become significantly greater than the two million tonnes per year now exported.

(3) The duty of making supplies of coal available, of such quality and sizes, in such quantities and at such prices, as may seem to British Coal best calculated to further the public interest in all respects, including the avoidance of any undue or unreasonable preference or advantage.

The above three clauses give British Coal extremely strong powers and clearly defined duties. The use of the powers is evident: the fulfilment of the public duties is not. British Coal has not, in practice, been accountable for its actions and has been continuously inefficient. Unlike other nationalised industries British Coal does not have a "watchdog" body.

Via these strong powers British Coal can (and has) frustrated attempts by third parties to improve the industry. (For example, the Monopolies and Mergers Commission recommendation in June 1983 that the statutory limit on the size of private opencast reserves should be raised to 100,000 tonnes has been completely ignored. The Government has taken no action to implement even this very modest proposal.)

The only way in which significant change will be brought about will be via changes in the Act. It is quite unrealistic to imagine that British Coal's management and labour will suddenly recommend ways and means of making the further very significant improvements which are open to the industry. The habit and practice of 40 years will be hard to overcome even in a reformed public sector monopoly.

Results of the Present Structure

The present situation, where one monopoly (British Coal) currently delivers 70 per cent of its output to one customer (the CEGB), has imposed a heavy financial burden on the nation. The artificially high price of feedstock to the CEGB, by virtue of its government-imposed requirement to purchase coal from this subsidised high cost source, has produced uncompetitively-priced electricity. Ultimately, the high price of electricity must have restricted the competitiveness of Britain's manufacturing industry relative to its main competitors, and must have contributed to Britain's industrial decline and rising general unemployment. Western Europe's most energy-rich country has gas, electricity and coal costs which are amongst the highest in Western Europe. In stark contrast, the privately-owned and competitive UK oil industry, from a standing start fifteen years ago, is now the fifth largest oil industry in the world, and the world's largest offshore producer (despite the adverse operating conditions of the North Sea). Structure and ownership are clearly the major determinants of efficiency/inefficiency in our energy industries.

[illegible]

The Legal Picture

Section 1(1) of the Coal Industry Nationalisation Act 1946 charges British Coal with three general duties -

(1) The duty of working and getting the coal in Great Britain, to the exclusion of any other person. There are only two exceptions to this clause:

(a) coal necessary to be dug and carried away in the course of activities other than colliery activities; and

(b) the getting of coal in accordance with the terms of a licence issued by British Coal [i.e. private mining].

(2) The duty of securing the efficient development of the coal mining industry (sic); and

3. PRIVATISATION

Stages of Privatisation

Privatisation of the industry could be sensibly carried out in two stages - the first would be a "liberalisation" of the industry, giving the private sector a greater involvement in coal production; the second would be "full" privatisation, with the sale of British Coal assets to the private sector on a diversified basis. Both actions would require changes to the Nationalisation Act: "liberalisation" would require that the phrase "to the exclusion of any other person" be deleted from Section 1(1) of the Act and changes to the clauses restricting labour force and coal reserves; whereas full "privatisation" would require that the 1946 Act be repealed in its entirety.

PRELIMINARY STAGE

The privatisation of British Coal as a group of diverse, self- contained operations to promote maximum competition and to involve entrepreneurial skills over a wide range and size of units, poses problems that have not had to be faced in earlier privatisation exercises. This suggests that the Department of Energy would benefit from additional assistance from specialists drawn from a wide range of backgrounds, with experience of good industrial relations practice, co-operatives, management buyouts, finance and venture capital, law, etc. There will also need to be those with special knowledge of the coal industry to advise on the best combination of viable self-contained units.

The Department of Energy, in carrying out privatisation will have three specific tasks.

1. The supervision of the immediate liberalisation of the coal industry;

2. the planning of the packaging and disposal by privatisation of the assets of British Coal; and

discuss, esp by analogy with onshore oil

3. setting up a new entity, designated the 'Crown Coal Commission', which would have a permanent, continuing role of holding and allocating coal reserves for future exploration and mining operations, and the administration of any residual social and environmental requirements of the industry.

After privatisation there would not need to be any entity charged with a price regulatory role since coal prices would be determined by market forces. However, the 'Crown Coal Commission' should be given an overriding duty of establishing and maintaining competition in the supply of coal in Britain. This should guide it in all its duties.

The Crown Coal Commission needs to exist in at least embryo form when the privatisation exercise is being planned since its detailed advice on how best to promote efficiency and competition should be invaluable.

The continued running of British Coal during the period when its operations are progressively being sold poses difficult but soluble problems. Special consideration will need to be given to motivating and rewarding management and staff in British Coal during the handover period. This would be a particular task for the attention of the specialist advisers already mentioned.

STAGE 1 - INITIAL LIBERALISATION

The initial liberalisation of the coal industry should be aimed at allowing growth in the small, existing private sector by removing the constraints placed upon it by the Act, and by British Coal's interpretation of the Act. Growth of the private sector could be achieved by:

(i) removing constraints on the private mining sector;

(ii) selling by tender coal tips to private sector companies;

(iii) selling by tender opencast operations reserves which are independent of present or likely future underground operations;

(iv) permitting contract mining in underground mines;

(v) permitting free trade in coal; and

(vi) removing certain legal restrictions.

These headings are considered in turn.

(i) <u>Removing Constraints on the Private Mining Sector</u>

The private mining sector is presently subject to the following constraints:-

1. In the case of underground mines, the underground labour force cannot "exceed or greatly exceed 30 men" (although a little flexibility is sometimes allowed in this area by British Coal). By contrast the average underground workforce in British Coal's collieries is 855.

2. In the case of opencast mines, reserves cannot exceed 35,000 tonnes of coal, or - in the case of adjacent sites - 50,000 tonnes. The Monopolies and Mergers Commission recommended in 1983 that the limit should be raised to 100,000 tonnes, but this has not yet been implemented. (The top 50 <u>privately</u> owned US coal mines all produce more than 50,000 tonnes <u>per week</u>!)

3. Private mines are required to pay wage rates similar to those agreed between British Coal and the mining unions. This could hold back employment and mining activity. Accordingly "plant bargaining" is required.

4. Private mines receive only "second tranche" (i.e. discounted) prices from the CEGB. Also, under the terms of the joint agreement between British Coal and the CEGB, the CEGB can only take 5 per cent of its coal from sources other than British Coal (including imported coal). This is clear evidence of one monopoly having a comfortable competition-restraining arrangement with another monopoly.

5. Underground private mines pay a royalty of £1 per tonne to British Coal, while privately owned opencast mines pay a punitive £16 per tonne! Incumbent British Coal pays no royalty!

The private sector, despite all these restrictions, has nevertheless produced profitable coal.

Generally, the private sector is working reserves or remnants which are too small or unfavourable to be of any interest to British Coal, but which nevertheless make a valuable contribution to the full exploitation of the country's coal reserves. It would be in the national interest if this contribution could be even greater, if the private sector were not so constrained and instead were permitted to expand. The Federation of Small Mines of Great Britain has recently commented that the joint agreement between British Coal and the CEGB may be in breach of several articles of the 1951 European Coal and Steel Treaty (Articles 65 and 66). It is always embarrassing not to be in compliance with EEC requirements, particularly where the aims of the EEC are to increase competition.

(ii) **Selling by Tender Coal Tips to the Private Sector**

The recovery of coal from old colliery tips, an activity restricted by British Coal, represents one of the cheapest methods of producing coal, since all mining costs have been already incurred during the initial working of the coal from which the tip is derived. In addition to providing cheap coal, the re-working of tips provides much needed employment in areas of unemployment and transforms derelict, and sometimes dangerous, land into a community asset.

Most old colliery tips are owned by British Coal. Tips are reprocessed, but only on a small scale, by private sector companies generally as contractors to British Coal. The coal is only used to "top up" production from deep mines: no attempt is made to maximise production despite its low costs. Under this system, a coal washing company cannot build up its own inventory of tips against which it can invest money in modern plant; if allowed to purchase tips, and hence invest in more sophisticated plant, such modern plant would maximise coal recovery from these tips and would ensure that the reserves were fully exploited.

(iii) <u>Selling by Tender Some Opencast Operations/Reserves</u>

There are areas of the country where opencast mining is totally separate from underground mining. In such circumstances the opencast mining operations and associated reserves should be sold to the private sector during the process of liberalisation.

Where there is interplay between surface and underground mining, or where such a potential can be demonstrated, such activities should be sold as groupings during the later privatisation process to ensure optimal use of coal reserves.

(iv) <u>Permitting Contract Mining</u>

Groups of workers (acting as companies or cooperatives) should be given the opportunity to mine coal at those collieries which British Coal has closed or is considering closing, and/or at collieries of a size too small to bear the overheads of British Coal. Such groups would contract to supply a stated tonnage of coal to British Coal at a stated price objectively determined. British Coal would supply technical services and lease mining equipment to the miners. The price would reflect the costs of such equipment rental and technical support.

In addition to contributing to the full exploitation of the country's coal reserves, this method of working would ensure employment for miners in areas of colliery closures. When a coal company in the United States closes an uneconomic but unexhausted mine, small entrepreneurial teams of miners welcome it. They see the closure as an opportunity to lease the seam from the company to work themselves. There is no reason to believe that UK miners would not wish to do likewise once a fair and reasonable scheme is worked out. It is in everyone's interest that more miners take a business interest in coal.

?

(v) **Free Trade in Coal**

Coal imports should be freed during the process of liberalisation, though there might be a case for phasing the removal of controls (which apply principally to power generation coal via the Joint Understanding between the CEGB and British Coal) over a short and clearly-specified period.

Despite the much lower pithead costs of coal mined in such areas as Australia, the United States and South Africa, imports need not be large in a liberalised UK coal market. The central coalfields in Britain have considerable transport cost protection from imports so that, even in a completely free market, the bulk of British demand would continue to be supplied from home sources.

Indeed, after privatisation, a more efficient British coal industry might well find additional export opportunities in Western Europe.

vi) Removal of Legal Restrictions

There are no legislative restrictions to remove before freer imports can be allowed. However, contract mining and the removal of constraints on the private sector are all moves which might involve changes in the Nationalisation Act. The selling of coal tips seems to throw up fewer legal problems, and this should form the starting point of any liberalisation of the coal industry.

An important and significant step would be the passing of an Act of Parliament to remove the clause "to the exclusion of any other person" from section 1(1) of the Act. This should be considered as the first step in the privatisation process of coal in the United Kingdom.

This completes our positive recommendations for liberalisation methods.

The Case Against Joint Ventures

For the sake of completeness we should consider joint venturing between British Coal and private sector companies since this has often been put forward as a sensible interim measure towards coal privatisation.

Although new ideas about production, distribution and marketing could penetrate the mining industry via joint ventures with British Coal, such joint venture arrangements seem very unlikely to be capable of satisfactory implementation. British Coal, which has had a monopoly for so long, would probably not participate enthusiastically any more than British Gas or the CEGB have co-operated on sharing facilities with private sector companies despite being required to do so by statute. Private investment would most likely be inhibited by the continued existence of a nationalised corporation, seen both as a subsidised competitor and also as a joint venture partner subject to government interference. In any case there would be little point in establishing joint ventures with a nationalised corporation which might soon be privatised. Finally, any resulting friction between British Coal and private joint venturing companies could well delay or even frustrate privatisation.

In sum, joint venturing looks superficially plausible but in practice would be a mistake.

STAGE 2 - PRIVATISATION

There is no need to wait until the coal industry, as presently constituted becomes profitable (if it ever does) before undertaking full privatisation of British Coal. Only if there were a case for privatising the industry whole (for instance, because it was a natural monopoly), which there is not, would the profitability of the industry as a whole be relevant. In striking contrast to British Gas, it is likely that much higher capital sums would be raised by splitting the industry, rather than by privatising it whole, (though capital raising should never be the main objective of privatisation). Indeed there might well be no demand to subscribe for shares in a monopoly which would be all too likely to persist in the inefficient non-commercial practices of British Coal.

Legislation would be required to privatise coal, involving removal of British Coal's exclusive right to "work and get" coal. Existing pits and opencast sites would be offered for sale. There would also need to be a system of licensing for new exploration and development. This function should be administered by the Crown Coal Commission.

The general objective of coal privatisation should be greatly to reduce the power of monopolistic forces in the British coal industry - British Coal's monopoly of coal production and the mining unions' monopoly of mining labour. Competing sources of coal supply should be established to bring benefits to consumers in terms of lower prices and enhanced security of supply and to the workforce in terms of more decentralised, less politicised bargaining over pay and other conditions of employment. Such benefits could not be obtained by simply shifting British Coal into the private sector as a monopoly with private shareholders, even assuming there were enough takers - an unlikely outcome.

A variety of forms of ownership should desirably be able to flourish in a privatised coal industry. Some smaller mines might best be run by workers' cooperatives; there could sensibly be management/staff buyouts for rather larger operations; but the larger and largest mines would almost certainly need to be owned by major mining companies because of the large capital sums and commercial knowledge required to run them. Varied forms of ownership would be more appropriate to an industry with varied conditions of production and a wide range of capital requirements rather than its centralisation under a state corporation or a private monopoly.

In contemplating privatisation, HMG needs to consider both existing operations and also future exploration and development activity.

Existing Operations

Existing operations, both opencast and underground, should be offered for sale by tender, individually or in groups but in the interests of competition no single company or consortium should be allowed dominance in any region. As part of its duty to establish and preserve competition the Crown Coal Commission would ensure that there was no such domination.

Potential investors, as already indicated, would be miners wishing to set up cooperatives, managers and employees wishing to buy out collieries, mining companies, or mining equipment manufacturing companies. There would be considerable advantage in offering some mines in combination with power stations and due consideration should be given to the existing coal transport arrangements between collieries and power stations when "packaging" assets for sale. Potential investors would probably be attracted by such "packages" and a possible problem of monopsony in power generation would be avoided. If there were a number of competing coal suppliers whose main market was in electricity generation, a centralised state-owned electricity supply industry would have very considerable market power. If, however, power stations were also to be in private hands - and state ownership or regulation in electricity supply were confined to the genuine natural monopolies of long distance transmission and local distribution to smaller consumers - the monopsony problem would be avoided. Quite apart from facilitating coal privatisation, there is a strong case in its own right for privatising the generation of electricity (the power stations) in Britain.

Some collieries which were perceived by private investors as "uneconomic" would doubtless remain unsold. They should not necessarily be closed, however. To the extent that there were justified social or strategic advantages in keeping them open, they could be kept in production explicitly at the taxpayer's expense. Any subsidies should be carefully considered, and be for sensible limited periods, and only be continued after thorough review. Even mines granted a subsidy could still be sold or managed privately.

Non-mining activities of British Coal should be sold off, also by tender.

Both in the initial sale of existing operations and subsequently, government action via the Crown Coal Commission to stimulate and maintain competition would be essential - otherwise the gains from privatisation could well be lost. There would be no point in having an industry which was dominated not by British Coal but by a small number of suppliers (whether domestic or foreign) acting in collusion. Privatising electricity supply would be another most important part of a policy of stimulating competition in coal and in the energy market generally.

Exploration and Future Development

To ensure that a healthly privatised coal industry can both come into existence and continue to thrive, the following would be necessary:

1. a scheme for allocating mining and exploration licences should be drawn up and administered by the Crown Coal Commission;

2. development of new, lower-cost reserves probably needs to be accelerated to lower the cost base, provide employment and perhaps give export opportunities;

3. planning procedures should be overhauled to ensure no undue delays (a subject deserving careful study); and

4. the existing centralised Research and Development activities, and safety research headquarters, should be funded by the mining companies. Parliament would continue to lay down, and the Mines Inspectorate Branch of the Health and Safety Executive, would continue to enforce safety standards within the industry.

4. SOCIAL AND LABOUR RELATIONS ASPECTS OF PRIVATISATION

The position of coal in the UK economy has changed very significantly since nationalisation. It now supplies only 32 per cent of home energy requirements, compared with 90 per cent forty years ago. Output has fallen from 218 to 104 million tonnes, manpower is down to about 126,000 compared to 717,000, and the number of active collieries has dropped from 958 to 133 (soon to be 110). Inevitably, in these circumstances, job security is a major concern of the industry's workforce.

The reduction of monopoly power, however, should on balance be employment-creating. Lower energy costs are likely to stimulate employment, especially in fuel intensive industries. In coal itself, it seems probable that consumer perceptions of monopoly power (resulting in expectations of insecurity of supplies and increasing prices) have reduced willingness to switch from other fuels to coal. Thus over a period of years, the diversification of supply sources which privatisation would bring is likely to increase coal demand and should also increase employment in "real jobs".

Decentralised, less politicised bargaining should give miners greater opportunities to participate in wealth created by their efforts. Proper systems of incentives and rewards would need to be provided by private owners - for instance, in the form of productivity-related pay, share purchase and share option schemes and improved pensions. Perhaps some minimum standards along these lines should be laid down in recognition of the industry's past poor labour relations and to ensure that labour relations improve after privatisation. Certainly any companies buying collieries would be well advised to offer profit participation, including shares on generous terms, to ensure a contented and prosperous labour force.

One aspect of privatisation deserves particular attention - namely the British Coal Pension Fund which is one of the largest in Britain. Upon privatisation, the appropriate part of the fund might be

(i) transferred to management and staff joining the many new owners; or

? (ii) kept in being and become the industry pension fund administered by a suitable body, probably the Crown Coal Commission.

This is a vital matter which deserves expert study. Either route might be acceptable. If the former route is chosen then no purchaser of an asset should be allowed to do other than guarantee at least equal benefits to those already existing. The latter route may be preferable, however, since it would permit free transfer of people within the industry (a known government priority), a clearly desirable aim if it is split up into competitive units, and one which may well commend itself to most employees.

5. SUMMARY AND CONCLUSIONS

The coal industry in the United Kingdom has not realised its full potential. Since 1946 it has been in the hands of a monopolistic supplier owned by the state. Many of the problems currently found in the industry would be best solved by dismantling the state monopoly, returning the industry to the private sector and allowing full and fair competition to be created between the separate entities.

British Coal is a high cost producer and because the CEGB is required to buy 95 per cent of its coal from British Coal, Britain's electricity costs have been unnecessarily high.

Despite the favourable price environment during 1973-1985 the output of British Coal has steadily fallen and it has lost market share in the UK to other energy sources. In contrast, output in most of the major producing nations has increased sharply over the same period and consumption in industrial nations has also risen.

Moreover, despite supported prices and a protected market in the UK, British Coal has made losses for most of its history and has required large subsidies from the taxpayer. Though some improvement has been seen since the 1984/85 strike, the coal industry will never achieve its full potential if it remains in the public sector, nor even in the private sector if it remains a monopoly.

Privatisation is the best means of reversing the industry's decline, but to do this the structure of the industry must be fundamentally changed. Coal is not a "natural monopoly" and competitive forces are the best means to ensure that coal is supplied as cheaply and efficiently as possible.

The privatisation of British Coal on a diversified basis to promote efficiency and competition raises new privatisation issues. Accordingly the Department of Energy will need the help of specialist advisers.

An additional permanent entity should be created, the 'Crown Coal Commission', to promote efficiency and competition. It would have a particularly important role advising the Department during the Privatisation Planning Exercise. It would have a continuing role administering social, planning and licensing matters, and should perhaps administer the industry pension scheme.

Privatisation can be phased in over a period by first immediately removing the legal constraints on the existing private sector, namely small mines and opencast sites. The most important step is the breaking up of British Coal operations into a large number of groups which would be sold by tender to whoever wished to purchase them. These may or may not be geographically based. Purchasers could be either individual companies, or consortia or even individuals. Moreover, employee buyouts and cooperatives should be encouraged, possibly with government aid, for the smaller collieries. Other non-mining activities should be sold off. Those activities which remained unsold would be retained by the government until either a subsequent sale or closure.

In all cases the Government should insist upon major profit participation incentives for all management and staff, and for pension arrangements at least as good as those presently existing, with full transferability within the industry.

It is essential that a private competing coal industry does not long have to face a monopsonistic electricity industry as its main customer. For the full benefits to be realised, the privatisation of the electricity generation industry into a number of competing entities is necessary.

An efficient private coal industry will ensure that the UK's coal reserves are most economically exploited. The major increase in efficiency which diversified privatisation would achieve should allow both the removal of subsidies and a fall in national energy costs. The sharp increase in productivity witnessed since the end of the coal strike and the profitability of much of the highly handicapped existing small private sector both indicate what should be possible. The prize from sensible privatisation for miners, management, customers, industry, suppliers and the Nation could be very large.

APPENDIX

NATIONAL COAL BOARD FINANCIAL RESULTS, 1980 to 1986 (YEARS ENDING MARCH)

(£ millions)

	1980	1981	1982	1983	1984	1985	1986
Operating profits (losses)							
Collieries	(122)	(107)	(226)	(317)	(595)	(1752)	169 [d]
Opencast	110	157	157	192	211	142	343
Other mining activities [a]	6	12	21	23	27	9	27
Non-mining activities [b]	26	17	5	3	(1)	(41)	(4)
Total operating profits (losses)	20	79	(43)	(99)	(358)	(1642)	535
Social costs less grants [c]	(17)	(29)	(61)	(49)	(74)	(78)	(170)
Interest	(184)	(256)	(344)	(364)	(467)	(520)	(437)
Other items	22	(1)	20	27	24	15	22
Deficit grant	159	149	428	374	875	2225	50
Surplus/(deficit) after deficit grant	0	(58)	0	(111)	0	0	0

Source: National Coal Board, Annual Reports and Accounts

Notes
(a) Rents, shipping terminals, etc.
(b) Manufacture of coke and smokeless fuel, chemicals, distribution of fuel and appliances, estates and land, engineering, computer services and income from related companies and partnerships.
(c) Costs incurred as a result of closing uneconomic capacity and the transfer or redundancy of employees which are met wholly or partly from government grants. In 1984 such government grants amounted to £270 million.
(d) After crediting £340 million for "strike recovery costs".

RP

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FINANCIAL SECRETARY
REC. 30 DEC 1986

19th December, 1986

Rt. Hon. Norman Lamont,
Financial Secretary,
H M Treasury,
Parliament Street,
LONDON SW1P 3AG

Mr D. Moore
PPS CST Sir P. Middleton
Mr Monck Mrs Brown
Mr Williams Mrs Diggle
Mr McIntyre Mr Ross Goobey.

Dear Norman,

PRIVATISATION OF THE BRITISH COAL INDUSTRY
THE SYKES PAPER

In general I agree with the thrust of this piece of work. The first steps in establishing a viable and competitive industry must be to relax the rules on private sector deep mining and to encourage the establishment of new privately-funded deep mine activities. Then you could consider selling off the open-cast reserves to several competing producers and breaking the national average price of coal.

May main criticism of the Sykes paper is based on a modicum of political caution. I wouldn't want to go to the barricades in favour of imported coal as this will be construed as market mad Conservatives favouring the demolition of British jobs to give preference to American and Australian mining activities. It is easier to dismantle the national average price of coal - to establish a competitive market - by allowing the pressures to come from within from a competitive British mining industry with a variety of investors and providers. Only be getting away from NCB dominance of marketing can you establish competitive conditions which in turn will create more demand for coal and for more investment and jobs.

There are immediate moves that can be made including the more rapid exploitation of open-cast reserves and more experiments with private mining and private open-cast ownership. Any one of these moves could help in reducing the cash cost of British coal to the tax payer as part of the public expenditure exercise, and need not await an election. All of these need to be viewed against careful consideration of NUM reaction to these moves.

Yours sincerely,

John Redwood

John Redwood

RT8.21

CONFIDENTIAL

b/f with response

FROM: A W KUCZYS

DATE: 2 January 1987

PS/FINANCIAL SECRETARY

cc PS/Chief Secretary
Sir P Middleton
Mr Monck
Mr D J L Moore
Mrs Brown
Mr M Williams
Mrs Diggle
Mr McIntyre
Mr Ross Goobey

THE PRIVATISATION OF THE BRITISH COAL INDUSTRY

The Chancellor has read the paper on coal privatisation which was handed to the Financial Secretary by Mr Sykes. He has commented that this is a useful paper. He thinks the key points which emerge are:

(i) The close connection between coal production and electricity generation - which should be privatised first?

(ii) In both cases, these are not - unlike electricity, gas and water transmission and distribution - natural monopolies: privatisation must therefore focus on the creation of competition and the breaking up of the present monopoly arrangements.

(iii) The achievement of this, which _may_ be best achieved by selling the various coal and or power station companies to corporate buyers, should take precedence over wider share ownership objecti~~ons.~~ves

(iv) Wider share ownership, by contrast, is a "natural" for water and the area electricity boards.

(v) The National Grid would probably need to be owned jointly by the various area electricity boards/companies.

(vi) The Chancellor is not convinced of the need for a Crown Coal Commission. In the case of oil, the job is done by Department of Energy.

2. The Chancellor was intrigued by the references to tip coal. He wonders how much economically recoverable coal at present exists on British Coal tips?

AWK

A W KUCZYS

2153/068

~~CONFIDENTIAL~~ AK

FROM: J J HEYWOOD

DATE: 7 January 1987

MR MOORE

cc: PS/Chancellor
PS/Chief Secretary
Sir P Middleton
Mr Monck
Mrs Brown
Mr M Williams
Mrs Diggle
Mr McIntyre
Mr Ross Goobey

I have minuted on all this: pse let me see a copy

Ch

Now attached AK 8/1

Thanks. Our 'mistranslation'! N

PRIVATISATION OF THE BRITISH COAL INDUSTRY

You were interested to know whether Mr Sykes of Consolidated Goldfields has shown his papers on coal privatisation to the Department of Energy.

2. I asked Mr Sykes who had seen the papers. He said that he had spoken to Mr Walker over lunch in early 1986 about his ideas and Mr Walker had told him that he was not interested in seeing any detailed papers on coal privatisation until after the next Election. This was "because of the risk of a leak on such a controversial subject". As a result of this, and Mr Sykes' belief that Mr Walker would not be sympathetic to the idea of breaking up the industry, he had not passed the papers to Energy.

3. Therefore, the only people who had seen the work were John Redwood, the Treasury and the Policy Unit. The latter had had some influence on the shape of the paper, having discussed the issues with Mr Sykes at an early stage. Mr Sykes said he would be happy to send the paper to anyone Treasury Ministers thought should see it.

4. I said that we would be interested to see the work Consolidated Goldfields had done on electricity, when it was completed. Mr Sykes, in turn, said he would be happy to give a slide presentation (lasting $1\frac{1}{2}$ hours) to Treasury officials or Ministers which highlighted the main features of the coal report.

5. Mr Sykes emphasised that Consolidated Goldfields would be very interested indeed in buying parts of the coal industry if the opportunity arose.

JH

JEREMY HEYWOOD
Private Secretary

ps3/60K

CONFIDENTIAL AM

28

FROM: A W KUCZYS
DATE: 8 January 1987

PS/FINANCIAL SECRETARY

cc PS/Chief Secretary
Sir P Middleton
Mr Monck
Mr D J L Moore
Mrs Brown
Mr M Williams
Mrs Diggle
Mr McIntyre
Mr Ross Goobey

PRIVATISATION OF THE BRITISH COAL INDUSTRY

In my note of 2 January, sub-paragraph (iii), "wider share ownership objections" should have read "... objectives".

AWK

A W KUCZYS

FROM: P C DIGGLE
DATE: 14 January 1987

1 MR M L WILLIAMS

2 CHANCELLOR

cc: CST
FST
Mr Monck
Mr Moore

BRITISH COAL : STOCKS

You asked (in your Private Secretary's note of 7 January) how much it would cost to transport British Coal's excess stocks from Scotland to power stations in the Midlands.

2. It is rather difficult to establish a reliable answer to this question since it would depend on the route and the form of transport chosen (probably rail or road) as well as on negotiations with the shipper. DEn's estimates are that the cost would probably come out in the range £10-12 a tonne. Since British Coal would sell any marginal extra coal to CEGB at third tranche prices, ie about £30 a tonne, this would mean that substantial losses would be incurred on such sales. Even opencast costs some £27-28 a tonne to produce.

PCDiggle

P C DIGGLE

4373/24 CONFIDENTIAL

NR

FINANCIAL SECRETARY TO THE TREASURY

FROM: J J HEYWOOD
DATE: 12 February 1987

MR M L WILLIAMS

1. Shd like [illegible] these, too.
2. There is much to be said for X's idea in addition. CEGB privatisation shd go hand-in-hand with CEGB restructuring [illegible] [illegible].

cc PS/Chancellor
PS/Chief Secretary
Mr F E R Butler
Mr Monck
Mr Moore
Mr Houston
Mrs Brown
Mr Lyne
Mrs Diggle
Mr Ross Goobey

COAL PRIVATISATION

The Financial Secretary was grateful for your interesting note of 10 February.

2. The Financial Secretary does not think any further contact with Consolidated Goldfields or with Mr Sykes would be appropriate at this stage, although he will read with interest the <u>written</u> pieces Mr Sykes has offered when they arrive.

J.H.

JEREMY HEYWOOD
Private Secretary

Papers
Pse

CONFIDENTIAL AR

FROM: M L Williams

DATE: 19 February 1987

CHIEF SECRETARY

cc Chancellor
Financial Secretary
Sir P Middleton
Mr F E R Butler
Mr Monck
Mr Burgner
Mr Moore
Mr Scholar
Mr Turnbull
Mrs Diggle
Mr Cropper
Mr Tyrie

A somewhat grudging reference to my achievement (as SoS Energy) in conclave with Mr J. Moore (then PSS [illegible]) in 1982, of the difficult condition of getting the NCB to reduce this venture to one-third of its former size & to reduce the commitment of govt from £40? below what the Treasury had previously agreed.

POINT OF AYR: COAL LIQUEFACTION SCHEME

Mr Walker has written to report his "intention to announce" the release of government support for BCC's coal liquefaction pilot project at Point of Ayr. Expenditure on this project, mentioned in Mrs Diggle's recent submission on the relevent vote (Class VI Vote 2), is not justified on its merits. For that reason we have withheld approval, and insisted that DEn Ministers write to you. But, because of past government commitments and wider political considerations, I recognise that it will be difficult for you to object to this expenditure. I therefore recommend that you should concur, making clear the basis on which you do so.

<u>Background</u>

2. In 1981, the then Chief Secretary gave approval to a government contribution of up to £5 million towards a pilot project on coal liquefaction which was to run at 25 tonnes a day. But this scheme ran into technical difficulties and, following an expert review, it was scaled down to 2½ tonnes a day to which the department offered 10% support, up to a maximum of £3 million. This revised arrangement was announced in November 1982 (without, incidentally, any consultation with the Treasury).

3. To date, £½ million has been released. Mr Walker is now intending to release the balance, pointing out that the conditions attached to this release have now been met. I accept this: BCC are making a substantial contribution themselves (45%); there is a substantial contribution (40%) from the European Community Energy Demonstration Programme; and BCC have secured a small contribution (5%) and technological support from a partner outside the industry. We attached some importance to an outside partner to stiffen BCC's project management and to ensure that the techniques explored were those most likely to prove cost effective. In the event, the choice of partner (Ruhrkohle Oil and Gas) is not perhaps ideal since their parent is subsidised by the German government; but the terms of their involvement are acceptable.

Economics

4. Our main worry is the justification for this expenditure. In our view, DEn's willingness to support an R & D project requires there to be some prospect that it will in due course be commercially, or at least eonomically, viable. This view is consistent with the department's own published objectives (see attached extract from the PEWP). But there is a negligible prospect of viability in this case.

5. The production of oil out of coal will be economic only if the price differential between oil and coal is larger than the cost of converting the coal to oil. At present prices, the gap is much too small. Since coal prices are unlikely to fall below the long run cost of supply, economic viability presupposes ~~at~~ sharply increased oil prices, and a sufficient increase to offset the edging up of coal prices that would follow. There is room for discussion as to where these curves cross, but it could be at an oil price over over \$60 (1986 prices), which is way above most commentators' projections for the next 30-40 years.

6. DEn now accept this argument, if pressed, despite some blustering in the past. They instead justify the project in

terms of the strategic insurance it offers; ie the UK would have the technology available against a rainy day (eg war, an unforeseen hike in oil prices, etc). Moreover other countries may be keener to exploit the technology for strategic reasons, eg Japan or South Africa, and BCC would be in a good position to sell into these markets (although of course there is no particular reason why they should chose to buy from BCC).

Wider Issues

7. I find these arguments unconvincing. But it would be difficult to withdraw our support:

1) The government has given a clear commitment. Moreover this commitment has been repeated since Mr Moore's 1982 announcement. For example, in April 1985 (and again without informing us) Mr Hunt said that the £2.5 million balance of the DEn's contribution remained on offer and was subject only to the NCB securing suitable participation from the private sector;

2) the government would have to justify withdrawing its support. We would have to point to the oil price fall, implying a deterioration in the economic prospects. But since the economic case was always weak, we could still be accused of inconsistency;

3) BCC remain committed to the project; and, we are told, because they see some prospects of commercial exploitation, as well as to molify the NUM, for whom coal liquefaction is a token;

4) BCC probably also see our support as all bound up with the Government's commitment to their longer term future; ie withdrawing support could mean a row with Sir Robert Haslam (although we may not be so committed as was MacGregor);

5) there is wider union, and some Parliamentary, support for similar reasons.

8. The sum of money involved is small, both in absolute terms and as a proportion of expenditure on the project. There is adequate PES and Estimates cover. A contribution to the scheme implies no commitment to support the larger scale pilot plant which would follow if this project were a success.

9. For all these reasons, I suspect that you would find it difficult to insist that Mr Walker does not make his announcement. But I would recommend that you make clear your scepticism of the merits of the project, putting the onus on Mr Walker. I have drafted the attached reply accordingly.

M L WILLIAMS

3.6 Department of Energy

£ million

Table 3.6.1 Analysis by broad economic category

	1981–82 outturn	1982–83 outturn	1983–84 outturn	1984–85 outturn	1985–86 outturn	1986–87 estimated outturn	1987–88 plans	1988–89 plans	1989–90 plans
Departmental running costs	16	17	24	26	26	26	26	30	30
Running costs receipts	−3	−3	−3	−4	−4	−4	−4		
Other public sector pay	147	157	165	166	180				
Transfers to the personal sector	48	80	190	200	563	537	201	170	140
Purchases of assets, goods and services	108	100	81	81	69	253	241	250	250
Transfers to the corporate sector	801	540	640	2,110	−163	−587	−555	−500	−660
Payments overseas	8	12	11	12	12	5	6	10	10
Total expenditure	**1,126**	**902**	**1,108**	**2,591**	**682**	**230**	**−85**	**−50**	**−240**
Contribution to total public sector capital spending(¹): —	*1,997*	*2,149*	*2,137*	*1,734*	*1,903*	*1,917*	*1,865*	*2,010*	*2,110*

(¹)For a general discussion of public sector capital spending see Part 2.

Departmental objectives

1. Within the framework of statute and of Government policy, the central objective of the Department of Energy is to encourage the maximum economic exploitation of the nation's energy resources and to promote the national interest in international relations in the energy field.

Regional and general industrial support

2. This expenditure amounting to some £15 million in 1987–88 covers grants under the interest relief grants scheme and coal firing scheme; European Coal and Steel Community guarantees; protection of oil and gas installations; and fuel supply arrangements.

Selective assistance

3. The main expenditure item on this programme is the Coal Firing Scheme which promotes conversion of industrial oil and gas boilers to coal by providing grants of up to 25 per cent of the capital cost. Since May 1981 grant commitments totalling £49 million have stimulated over 400 conversions with project costs totalling over £250 million and have generated 2·75 million tonnes a year of extra coal burn. New applications have dropped sharply following the fall in oil prices. The scheme closes to applicants in June 1987.

4. Final payments are expected to be made in 1988–89 under the offshore supplies interest relief grant scheme (closed to applicants since 1979).

Other support services

5. The department contributes about £0·5 million a year to the cost of surveillance of offshore oil and gas installations, mainly undertaken by the Ministry of Defence.

Scientific and technological assistance

Research and development

6. The department's vote-funded research and development forms a single budget. The Secretary of State establishes priorities for research on the basis of advice from his Advisory Council on Research and Development. The Council keeps the department's R&D expenditure under review against its objectives. An increasing proportion of energy R&D expenditure is being contributed by non-Government sources.

7. The overall objective is to encourage research and development that would not otherwise be undertaken in order to:

(i) contribute to the economic exploitation of the UK's natural energy resources;

(ii) establish economic options for secure and efficient energy supply, distribution and use of energy;

(iii) as part of the Government's industrial strategy, to encourage energy industries to develop new technologies related to the supply, distribution and use of energy for the domestic and export market.

(iv) enable the department to carry out its statutory and regulatory responsibilities.

Within this framework the main areas of research are discussed below.

3822/7

~~CONFIDENTIAL~~ NC

DRAFT LETTER FROM CST TO SECRETARY OF STATE FOR ENERGY

POINT OF AYR: COAL LIQUEFACTION SCHEME

Thank you for your letter of 17 February.

I am unconvinced of the case for th~~e~~is~~e~~ project~~s~~. It seems to me that, if we were looking at it for the first time today, the prospect of economic exploitation of this technology is so remote that we would not be able to justify support. I would therefore question whether in fact it fits within the aims of your R&D programme.

I nevertheless recognise that the Government is committed to support the project, and that the conditions previously required have been met. If you feel that this commitment, and wider considerations you mention, are overriding I will not press my concern further. I take it that BCC will be left in no doubt that the Government's support to the pilot scheme will not imply any contribution to any future phase of the project.

It would be helpful if your officials could clear the terms of any announcement with mine.

JM

4413/18

~~CONFIDENTIAL~~ AM

Sir: From P C Diggle

Date 10 April 1987

1. MR ~~MOORE~~ DW 10/4

2. CHIEF SECRETARY

cc Chancellor
Mr F E R Butler
Mr Monck
Mr M Williams ~~for~~
Mr A White
Mr Sharratt

When I was Bonn & looking @ the figs, it was the case that the German subsidy per tonne of deep-mined coal was 9 times ours. It may be still; but I don't know what follows from that (esp since G is a net subsidy from with a much smaller coal industry) M.

BRITISH COAL

This note tries to answer the questions arising out of your dinner with British Coal last week, with the exception of the point on lignite, on which ST3 will be commenting. (Miss Rutter's note of 6 April).

Social grant

2. Social grant is an umbrella term for the group of grants payable in support of British Coal's rationalisation costs other than redundancies. It covers assistance with pit closures, concessionary coal payments to redundants, and support for the additional burden on the mine workers' pension fund.

3. It is one element of finance available to British Coal to fund its EFL. The others are deficit grants and borrowing. Recent figures are set out in table 1. In practice borrowing is the residual, because:

(a) social grant payments are determined by actual social costs - ie pit closures, pension deficits etc; and

(b) deficit grant payable reflects British Coal's actual losses after social grant in the year concerned (with adjustments to reflect actual cash need).

German subsidies

4. The Board claimed that the German coal industry gets more support than the UK, in particular by way of protective agreements with the steel and electricity industries. It is certainly true that the German coal industry gets significant help from these sources: the IEA quotes for 1985 subsidies of (DM m):

Investment aid, special depreciation and other production subsidies	360
Subsidy for coking coal production	1150
Support for purchasers of coking coal:	
- domestic steel industry	22
- export	8
3.5% levy on electricity sales	1885
(funds a subsidy to coal-burning electricity utilities to compensate for higher price of German coal).	
Total	3425

5. In sterling terms this amounted to about £10 a tonne in 1985.

6. Comparable UK figures quoted by the IEA for 1985-86 are (on an accruals basis, ie not the same as public expenditure in cash) (£m):

Deficit grant	50
Social grant	513
Redundant mineworkers payment scheme	566
Coal firing scheme	12
Total	1141

7. This amounts to £11 a tonne, ie rather more than Germany.

Moreover it leaves out the premium paid by the electricity industry under the BCC-CEGB agreement for buying British Coal's output at prices higher than international levels. Arguably this added some £¾bn, taking the total support rate to some £18 a tonne, ie approaching double the German level. SO the Board's proposition seems not to be true.

8. There is, however, an important distinction about the quality of support in the two cases. The German subsidies are all structural props disigned to make it possible for an uneconomic business to continue indefinitely. Moreover, the pressure is upward (eg the electricity levy rose 1% to 4½% in 1986) and there are few incentives to rationalise. By contrast, only part of our support arrangements are related directly to production: deficit grant (to end in 1987-88); the coal firing scheme (ends June 1987) and the premium paid by the electricity industry (declining, but slowly). The rest all aid restructuring directly. For this reason the IEA broadly commended our approach(though with a reservation about the relationship with the CEGB) and criticised the German arrangements quite strongly.

Loss making sales

9. British Coal claim that only 20% of current output is sold at a loss compared to 60% 4 years ago. We do not have information readily available which would enable us to check this assertion. It sounds a little optimistic, in that the assumptions underlying the IFR projected some 30% of sales at a loss during 1987-88. But plans have been tightened since then and production costs cut by further redundancies, so the 20% claimed could be true.

10. Another crude check is to compare the average loss per tonne. In 1983-84 it was almost £7. This year is should fall below £1, corroborating that a dramatic transformation of the kind described is taking place.

11. It is worth viewing this achievement - worthwhile though it is - in an international perspective. At current exchange rates, British Coal's average selling price last year was still

about 25% higher than internationally traded coal, even taking account of delivery costs. This reflects the substantial premium paid by the CEGB.

Capital reconstruction

12. British Coal mentioned the possibility of ending some grant support in return for writing off debt to lower interest costs.

13. Projections of the relevant grant and interest payment flows to 1989-90 are shown at table 2. The figures are somewhat uncertain since they depend on interest rates and actual social costs, including the extent of pit closures and numbers of redundancies in the years concerned, which are still to be decided.

14. However, it is clear enough that the deal would be a bad one from the point of view of the exchequer. It would be difficult to disengage the government from social grant commitments, which are written in to previous legislation and would be emotively opposed. It would be comparatively easy to cease payment of the new restructuring grant (set up under the recent legislation), because this grant requires an annual order specifying the rate payable. So British Coal were probably suggesting exchanging debt service for restructuring grant only. This would leave the exchequer worse off by some £400m a year if all the debt were written off.

15. It might, however, be possible to incorporate some element of this kind into a possible future restructuring. You will recall that we have provisional agreement from Mr Walker that there will be no question of restructuring until break even is achieved (ie next year on current projections) and that it will not involve relieving British Coal of the need to service its existing capital. In this kind of framework it would be possible to exchange lower grant for some debt write-off. But if we did so we should need to be satisfied that British Coal's remaining capital base was not trimmed to so low a level as

to fail to reflect its assets. Since these have been falling with pit closures, a trade off of this kind might well be an attractive option.

P C Diggle

P C DIGGLE

CONFIDENTIAL

From: P C Diggle
15 September 1987

cc CST
Mr Monck
Mr Moore

1. MR WILLIAMS 15.9

2. CHANCELLOR

Thanks. Clearly the route would be either (a) or (b) — the CEGB closing the PX ... I think PX is raising the cost either way. If (as is likely) the overtime ban takes place the case for going immediately for oilburn is pretty strong. N.

COAL STOCKS

I understand you are interested in the cost of restoring the CEGB's autumn stockbuild programme to its normal pattern.

2. You are aware of the Prime Minister's concern about the slowdown in CEGB's seasonal stockbuild. On present plans pre-winter stocks at power stations will reach only about 25.5mtonnes against the target of 27mt. The slippage is as much the result of lower nuclear output (requiring more coalburn at the power stations) as the partial overtime ban at British Coal.

3. The CEGB claim that 25.5mt now will still give 9 months' strike endurance cover, as stocks of 27mt were planned to do when agreed two years ago. This is partly because nuclear output is higher (though not as much as it should be) and partly because coal-fired stations are more efficient (eg a 1.6% improvement in thermal efficiency last year alone). In addition, CEGB know from the experience of the last strike how to burn oil at coal stations to eke out what coal is available if supplies are restricted.

4. If, nevertheless, it were felt imperative to regain the 27mt target, the cost would depend on the method used:

(a) If CEGB chose to burn more oil to conserve coal, any additional cost would be pretty trivial. There might even be a modest saving.

(b) If CEGB bought more coal at the margin from BCC, it would rundown pithead coal stocks to closer to economic levels, probably ending the financial year at about 9mt if output is not too greatly reduced by the overtime ban. The stockshift would be public expenditure neutral since the transfer of some #45m from the ESI to BCC, would worsen the threatened ESI overspend (cashflow is already some #233m adrift of the EFL) and simultaneously improve BCC's cash position (a projected overspend of some #125m).

(c) If CEGB took the provocative line of importing coal, it might be possible to get sufficient coal to supply the deficiency for as little as #30-35m delivered, if CEGB are able to deal as well as they did earlier in the summer. This would add to public expenditure directly through the ESI's EFL, because there would be no countervailing benefit to BCC's cashflow such as would happen in (b).

5. I hope this is the information you are looking for.

P C Diggle PC Diggle

6

RJ8.35

~~CONFIDENTIAL~~ NR

PLP

FROM: J M G TAYLOR

DATE: 16 September 1987

MRS DIGGLE

cc PS/Chief Secretary
Mr Monck
Mr Moore
Mr M L Williams

COAL STOCKS

The Chancellor was grateful for your minute of 15 September.

2. He has commented that the route used would be either for the CEGB to burn more oil to conserve coal, or for them to buy more coal at the margin from BCC and run down pithead coal stocks to closer to economic levels. The CEGB clearly prefer the first option. It is reassuring that there is no public expenditure cost either way. If (as is likely) the overtime ban takes place, the case for going immediately to oil burn is pretty strong.

J M G TAYLOR

Ch discussed with MP.

CH/EXCHEQUER

REC. 18 SEP 1987

ACTION MRS DIGGLE

COPIES TO CST, SIR P MIDDLETON, MR F E R BUTLER, MR MONCK, MR ANSON, MR D.J.L. MOORE, MR M.L. WILLIAMS, MR BURGN, MR HAWTI, MR GILM

~~CONFIDENTIAL~~ AK

Ch This is apparently what Mr Parkinson wants to see you about on Monday

18/9

Reference No E 0398

CHANCELLOR OF THE EXCHEQUER

E(CP)

18/9/87.

I understand in confidence that Mr Parkinson will approach you very shortly to ask that E(CP) should not, as intended, discuss competition in coal at the meeting now arranged for 2 October.

2. Mr Parkinson will say that he does not want to worry Sir Robert Haslam about this subject now, when he has his hands full with the NUM dispute and other matters on which he will come under pressure from the Government, such as the CEGB supply arrangements. He may also say that it would be fatal if any hint got out at present that the Government would like to introduce more competition on coal.

3. I think it would be a pity if this subject was dropped from the agenda. The coal paper is one of the most important of those which, at the last E(CP) meeting, you said should be ready by September. The remit goes back nearly a year to December 1986, and it was Mr Parkinson himself who suggested at the last meeting that it should cover not just opencast, as originally intended, but also private licensed mines. If Mr Parkinson is concerned about relations with British Coal, and the possibility of a leak, he could circulate a paper giving only provisional views, subject to consultation with the Board and a firm recommendation against taking any action at present. I understand in confidence that he had a draft paper some time ago, so this would be practical for him.

Minutes enclosed

4. Another point is that the Policy Unit at No 10 have shown great interest in this paper. They might attempt to interest the Prime Minister if it slipped from the agenda.

5. As to the other papers, those which are on course for the meeting on 2 October are from

- The Lord Chancellor on restrictions in the legal profession. This is the most important.

- The Trade and Industry Secretary on restrictions in the professions generally.

- The Environment Secretary on possibilities of greater private sector involvement in local authority refuse disposal sites.

6. Other papers which we have just heard may slip, after promises to the contrary, are from:

- The Social Services Secretary, on competition in the pharmaceutical industry.

- The Trade and Industry Secretary, on radio frequency spectrum management, and needletime. The fault here, at least on the second, may be with the Home Office, who have not yet responded to a DTI draft.

7. I shall chase the Departments concerned before the meeting. An agenda limited to the three papers in paragraph 5 would be adequate but the doubts over the other papers strengthen the case for keeping coal on the agenda if at all possible.

G W MONGER

Cabinet Office
18 September 1987

~~CONFIDENTIAL~~ AK

From: P C Diggle
21 September 1987

1MR WILLIAMS 21-9

2. CHANCELLOR

Ch.
For your talk with Mr P this afternoon.
JT 21/9

cc CST
Sir P Middleton
Mr FER Butler
Mr Monck
Mr Moore
Mr Burgner
Mr Gray

E(CP): COAL

Mr Monger warns, in his minute of 18 September, that Mr Parkinson is likely to suggest postponing the long awaited paper on injecting competition into the coal industry. We agree with Mr Monger that you should resist, though it would do no harm to take the issue in a more limited group if that would assuage Mr Parkinson's anxieties.

2. Of course Mr Parkinson is right that BCC management will need to devote effort into dealing with the NUM overtime ban starting today. But it would be folly to neglect the deeper structural questions facing the coal industry in the heat of the current crisis, if indeed it is a crisis. British Coal has lurched from one short term solution to another in the two and a half years since the strike ended, making strategy up as it has gone along. By this means it has robbed ministers of adequate input into the real decisions and now finds itself with an inappropriate long term strategy.

3. Your best card in resisting Mr Parkinson is to link the E(CP) paper with the strategic work connected with electricity privatisation. It was agreed at Chequers only last week that it would be necesary to liberalise imports of coal by or shortly after the privatisation of CEGB or its succesor(s). That will be a massive leap into a new competitive environment for British Coal, and the sooner they start to adjust to competition the better. The E(CP) initiative was aimed at beginning that process.

The E(CP) paper was mentioned at Chequers.

4. Mr Parkinson may argue that an E(CP) discussion of liberalisation of competition in the coal industry would be inappropriate given the strategic review just about to begin. This is misleading. The sooner the process starts the better. There will never be an ideal time to tell the NUM that their stranglehold over coal production is weakening further. There is no point in entrenching their position for longer.

5. Mr Parkinson's strongest argument is the danger of aggravating the overtime ban by a modest liberalisation initiative now. There is certainly a danger that Mr Scargill could inflate any move into a scare story. But many miners have little stomach for a prolonged fight since they are still recouping the losses they made in the 1984-85 strike. You might probe Mr Parkinson about how serious the threat really is.

5. If it would help Mr Parkinson in dealing with Sir Robert Haslam, you might offer to take the coal liberalisation paper in a small group restricted to those ministers who have an interest in

electricity privatisation: say Mr Rifkind, Lord Young, Mr Parkinson and yourself. This would limit the risk of leaks if that is what is worrying Mr Parkinson.

6. The joke about the fuss is that the paper Mr Parkinson has prepared proposes fairly minimal action to promote domestic competition. It would avoid legislation, so British Coal would still be vested with substantial monopoly extraction rights. The main change on offer would simply be raising the limit on the volume of private production, possibly only marginally. We have given Mr Parkinson's officials lukewarm encouragement for this approach, regretting that it does not go further.

However, we have yet to be properly consulted.

P C Diggle

P C Diggle

I agree with this advice. Even if there was a leak, it is probably helpful to be able to set Ministers' discussions against the background of competition policy generally. That would be less inflammatory than leaks of a new "strategic review", and these issues certainly have to be discussed now if the Chequers conclusions mean anything. That said, a sub-group of Ministers concerned would be acceptable.

21.9

ps3/17T

~~CONFIDENTIAL~~ NR

BF 30/10

FROM: J M G TAYLOR

DATE: 7 October 1987

MRS P C DIGGLE

cc PS/Chief Secretary
Sir P Middleton
Mr F E R Butler
Mr Monck
Mr D J L Moore
Mr Burgner
Mr Gray

E(CP): COAL

Thank you for your briefing note to the Chancellor. As you may have seen, the E(CP) meeting on 2 October was cancelled (because of the Lord Chancellor's illness).

2. The Chancellor spoke to Mr Parkinson about the handling of the planned paper on coal. It was agreed to take this in a more limited forum than E(CP). The Chancellor has in mind a group consisting of himself, Mr Parkinson, Lord Young and perhaps Mr Ridley. Mr Rifkind may also be invited to attend.

3. The next step is for Mr Parkinson to write to us setting out his proposals. When we receive that letter this office will arrange a meeting.

JT

J M G TAYLOR

SECRET [redacted] Copy No 1 of 12

SECRETARY OF STATE FOR ENERGY

SECRETARY OF STATE FOR ENERGY
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CH/EXCHEQUER	
REC.	28 OCT 1987
ACTION	Mrs P Diggle
COPIES TO	PS/CST ~~PS/~~FST, Sir P Middleton, Mr F E R Butler, Mr Monck, Mr D J L Moore

Mr Burgner
Mr P Gray.

For meeting

Ch/ Shall we now organise a meeting – Mr Parkinson, Ld. Young, Mr Rifkind (and Mr Monger from Cabinet Office)?

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

28th October 1987

Dear Nigel

LIBERALISATION OF THE LICENSED COALMINING INDUSTRY

At the Chequers Seminar on 14 September it was suggested that E(CP) should consider the possibilities for removing the present restrictions on coal production by the private sector. As we have since agreed, it would be wrong at this stage to put a paper to E(CP), which would necessarily have to discuss issues which are sensitive in terms of industrial relations. Moreover, I should be much opposed to any action which would distract Bob Haslam from his crucial task of improving the efficiency and profitability of British Coal's core business.

However, I agree that we must continue to work on the possibilities in this area. I have accordingly asked my officials to prepare the attached paper; they have also had some helpful discussions with your own people. I hope that the paper will serve as an acceptable basis for a meeting between us and the other recipients of this letter.

I accept the judgement in the paper that it would be wrong to embark on a fundamental recasting of the present legislative framework outside the context of privatisation of the BCC. To do so would entail enormous upheaval and considerable administrative expense. It would take up a great deal of the time of senior British Coal management. It would stir up the inevitable controversy that will be associated with the privatisation of the coal industry, when our priority will be to make the privatisation of the esi a success. And it would do all this without bringing any great economic benefits.

However, I agree that it would be worth raising the limits on licensed coal production, as officials propose, when the legislative programme permits. I also agree that it would be worth exploring the other possibilities mentioned by officials, which do not require legislation. I shall report more fully on these aspects when we meet.

SECRETARY OF STATE FOR ENERGY

I am sending copies of this letter to David Young and Malcolm Rifkind, and to Sir Robert Armstrong. I should be grateful if you and they would ensure that the papers are seen only by those with a clear "need to know".

Yours Ever,

Cecil

CECIL PARKINSON

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LICENSED COAL PRODUCTION BY THE PRIVATE SECTOR

NOTE BY DEPARTMENT OF ENERGY OFFICIALS

1. This note discusses the possibility of increasing competition and efficiency in the UK coal industry by removing or reducing restrictions on licensed coalmining by the private sector.

Background

2. Under the Coal Industry Nationalisation Act 1946, as amended, virtually all unworked coal in Great Britain is vested in the British Coal Corporation (BCC). The BCC:

(a) have the statutory duty of making supplies of coal available in such quantities and at such prices as may seem to them best calculated to further the public interest;

(b) have the statutory duty of securing the efficient development of the coalmining industry;

(c) have the sole right of searching and boring for coal in Great Britain; and

(d) subject to certain exceptions, have the sole right of working and getting coal in Great Britain.

3. The exceptions are that the BCC may:

(a) license production from deepmines so long as the numbers employed there below ground are at no time likely to exceed, or greatly to exceed, 30; and

(b) license production from opencast sites so long as total (not annual) production from a site is unlikely to exceed, or greatly to exceed, 25,000 tonnes.

The BCC's licences under these provisions lay down conditions, including conditions as to royalties. The present level of royalties is £1/tonne (deepmined) and £13.50 per tonne (opencast). Total licensed coal production is currently about 2.6 mtpa. Further details are given in Annex A.

4. In 1981, following complaints from the licensed sector, and pressure from the Government, the BCC and representatives of the licensed opencast sector agreed on a number of relaxations, set out in the "Five Principles". The text of this is at Annex B.

5. The present arrangements have been criticised in several

ways, of which the following are the most important.

(a) That the present system unduly restricts competition, by making the BCC sole judge of whether to issue licences (and on what conditions), and by setting the limits on licensed operations unduly low. The Monopolies and Mergers Commission, in their 1983 Report on the Coal Industry, recommended increasing the limit on opencast sites to 100,000 tonnes.

(b) That the BCC operates the system unfairly, particularly by setting royalties unreasonably high.

(c) That the Central Electricity Generating Board (CEGB) under their Joint Understanding with the BCC, allow too little scope to the private sector.

Objectives

6. The fundamental objective is to create an energy market, including the market for coal, which allows consumers access to supplies of energy at competitive prices and to choose whatever supplies provide them with what they regard as the best combination of convenience, cheapness, and security. It is arguable that a necessary condition for this is to privatise the UK coal industry in a way which fosters competition. However, Ministers have stated publicly that they have no plans to privatise the BCC during the present Parliament; and we have assumed in this note that they do not wish at this stage to pursue the privatisation of the BCC's main business.

7. Within that assumption we have examined possible ways of increasing competition in the coalmining industry and, in particular, of increasing the availability of low-cost supplies of coal. They fall under the following headings:

(a) changes requiring substantial recosting of the present legislative framework;

(b) other changes requiring legislation; and

(c) changes not requiring legislation.

RECASTING THE PRESENT LEGISLATIVE FRAMEWORK

Vesting Coal in the Crown

8. The transfer of ownership of unworked coal, and with it the rights of licensing and royalty-collection, from the BCC to the Crown would certainly deal with the criticism that the present system is basically unfair (paragraph 5(a) above). It was recommended by the Select Committee on Energy in their Report earlier this year. But it would be a very far-reaching move. Carrying out licensing and royalty-collecting functions would require the recruitment of large numbers of scarce specialist staff: the functions could not be contracted out to the BCC,

since they would be among the competitors for licences. It would also be essential to delimit the BCC's existing rights to work coal; this would be a large and time-consuming undertaking. And there would be strong political controversy, since it is generally recognised that the transfer of ownership is a necessary step on the road to privatisation.

9. Outside the context of privatisation, the change would do little to increase the availability of low-cost coal. As explained in more detail in paragraph 11 below, the main limitations on opencast production are the lack of suitable deposits in the UK, and the planning system; and in UK conditions deepmined pits operating with substantially less capital and manpower than the BCC's pits would not add significantly to production.

Privatise Opencast Production

10. It is often suggested by outside commentators that the "opencast business" of the BCC should be privatised in advance of privatisation of deepmined operations. Such suggestions largely rest on a misunderstanding. The BCC has no "opencast business", but rather a continually changing collection of sites capable of being worked by opencast methods (the average lifetime of such sites is only four years). The rights to work such sites could not be sold far ahead, especially as the BCC alone have the geological information required to bid for them sensibly. To prevent the BCC from working the sites would require drastic changes in the present legislative framework; and since the definition of the sites, if it could be framed at all, would vary over time with the technology and economics of opencast operations, it is likely that the only workable method would be to transfer the ownership of all coal to the Crown, as discussed in the preceding paragraphs.

11. Moreover, this approach would do little or nothing to increase opencast output. The BCC's present strategy is to increase opencast production, which is generally far more profitable than deepmining, to the maximum extent. They are limited partly by the lack of suitable sites in such a built-up country as Great Britain, and partly by the reluctance of many local authorities to grant planning permission for opencast sites. There is no reason to suppose that local authorities would be more willing to license private operators: if anything, the reverse is true.

12. Finally, the approach would increase competition only in the marketing of coal, not in its production, since all opencast production by the BCC is already in the hands of private contractors, chosen by competitive tender. It might generate some downward pressure on prices (though a more effective way of doing this would be by increasing imports of coal). Against this, it would tend to weaken the finances of the public sector: the present system automatically captures the whole of the economic rent from the great bulk of opencast coal production for the ultimate benefit of the taxpayer; it would be more difficult to do this if all opencast production were in private hands.

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OTHER CHANGES REQUIRING LEGISLATION

Increasing the Limits on Licensed Production

13. The BCC work very few opencast sites with prospective total production of less than 300,000 tonnes. There is therefore a good case for increasing the statutory limit on licensed opencast production from 25,000 tonnes to, say, 250,000 tonnes. A similar increase in the limits on licensed deepmined sites would increase the limit on men working underground from 30 to 300. This is well below the numbers employed at the BCC's pits. The changes would require legislation but would be technically straightforward. They should bring about a modest, but useful, increase in low-cost coal production without raising the difficult institutional and political issues posed by the more sweeping changes discussed in paragraphs 8 - 12 above.

Abolishing the Limits

14. To go further, and abolish the limits on licensed production, would raise those issues. Operators wishing to work large opencast sites would be in direct competition for them with the BCC. (So, in principle, would anyone wishing to open a large deep mine. However, in present circumstances that possibility is more remote.) They would find it hard to accept that the BCC should be the licensing and royalty-collecting authority for such sites. The BCC, for their part, would argue - with justice - that extensive licensing of other operators would be inconsistent with their statutory duties (paragraph 2 (a) and (b) above). Moreover, for the reasons outlined in paragraph 11 above, removing the limits would do little or nothing more than raising them to increase the production of low-cost coal.

CHANGES NOT REQUIRING LEGISLATION

15. It would be possible without legislation for the BCC to make the existing system more liberal and transparent. The most promising possibilities seem to be as follows.

(a) It would be reasonable to ask the BCC to consult Ministers before setting general levels of royalty, and to be more willing to negotiate reductions in royalty in particular cases where unforeseeable changes in circumstances made it impossible for an efficient operator to make a profit.

(b) It would also be reasonable to ask the BCC to publish their criteria for awarding licences.

(c) It might be possible to build on the existing "Five Principles" so as to issue licences for sites adjacent to existing sites for further amounts of 25,000 tonnes (though there are legal problems here which need careful consideration).

(d) It would be possible to explore with the BCC the possibility of removing the requirement in current licences for deepmined operations to pay BCC wage rates.

Energy Ministers are discussing these possibilities with the Chairman of the BCC.

16. Finally, there is the CEGB's undertaking to the BCC that they will take 95% of their annual coal requirements from the BCC. The remaining 5% amounts to less than 4 mtpa; and the private sector has to compete for this business with imports. Reducing 95% to, say, 92% would greatly increase the scope of the private sector and remove one of their main grievances. However, the undertaking is a key element in the deal between the BCC and the CEGB. For the Government to press the CEGB to change it would call into question the line which Ministers have repeatedly taken in public that the deal is a commercial arrangement between the two industries, and would be strongly criticised by the BCC on the grounds that the Government was intervening in normal commercial negotiations in order to disadvantage them.

CONCLUSION

17. Fundamental changes in the present legislative framework outside the context of full privatisation of the coalmining industry would lead to great upheaval and political controversy and would be unlikely significantly to increase low-cost coal production. However, legislation to increase the present limits on licensed coal production to, say, 250,000 tonnes (opencast) and 300 men underground (deepmined) would be technically straightforward and would raise fewer problems, while probably achieving some modest increase in low-cost production. It would also be possible in advance of legislation to explore with the BCC a number of ways of making the present system more liberal and transparent on the lines indicates in paragrah 15 above. A reduction by the CEGB in the proportion of their coal requirements which they undertake to buy from the BCC would significantly increase the scope for the private licensed sector, and remove one of their chief grievances; but the difficulties of intervening in what the Government has always publicly represented as genuine commercial negotiations between the two industries would be substantial.

(a) Licensed Deep Mines: Because of size restrictions, licensed deepmines are all drift mines. There are 169 at present, of which 109 produce high value anthracite in Wales. They pay £1.00 per tonne royalty (around £0.04p per G/J) to British Coal. Most of the other mines supply power stations, particularly the SSEB. Production has risen from 290,000 tonnes in 81/82 to 784,000 tonnes in 86/87. Total manpower is around 1,600.

(b) The Licensed Opencast Sector: Production in this sector has increased steadily from 0.8mt in 1981/82 to 1.8mt last year; but the recent fall-off in new applications suggest that this trend will be reversed. The sector consists largely of small businesses working 85 small sites, and employing 1,500 men. Its primary market is power stations; but in both the North-East and particularly Scotland there is an important presence in the small industrial market. Its margins are almost certainly being squeezed. A royalty of £13.50 per tonne (0.53p per GJ) is payable to British Coal (unless reduced for a particular site) and receipts from CEGB have been negotiated downwards to £1.39-1.45 per GJ for delivered coal. With transport costs at £0.09-0.23 per GJ a balance of 0.63p-0.83p per GJ is left for mining and other costs and for profit.

Annex B

LICENSED MINES AND OPENCAST SITES

In 1981, following discussions between John Moore (the Parliamentary Under Secretary of State at the Department of Energy), the National Coal Board and the National Association of Licensed Opencast Operators, the NCB agreed:

- first, to licence opencast sites with up to 35,000 tonnes of workable reserves and to resume the practice of considering a second licence of adjacent sites bringing the total tonnage of contiguous reserves under licence to around 50,000 tonnes, in effect doubling the present limit;

- secondly, to exercise the greatest possible flexibility on the maximum size of licensed deep mines, giving sympathetic consideration to applications for mines employing over 30 persons underground.

- thirdly, to phase out the practice of requiring many opencast licensees to deliver their coal to the Board by offering all new licences free from any delivery requirements;

- fourthly, to set royalties at levels which will permit efficiently - managed operators to develop their business profitably;

- fifthly, to reduce royalties for new licences in any case where accounting evidence is provided which demonstrates that profit expectations would otherwise be cut to unreasonably low levels.

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SECRETARY OF STATE FOR ENERGY
THAMES HOUSE SOUTH
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CHIEF SECRETARY
REC. 01 NOV 1987
ACTION Mr. M. L. Williams
COPIES TO CST, FST, Mr Butler, Mr Monck, Mr Burgner, Mr Moore, Mr Turnbull, Miss Diggle, Mr Tyrie, Mr Call

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

29 October 1987

Dear John,

BRITISH COAL EFL 1987/88

In his letter of 6 March to John MacGregor, Peter Walker warned that British Coal were almost certain to need a higher EFL for 1987/88 than the £727m in the Public Expenditure White Paper. There has, however, been continuing uncertainty about the precise amount of the increase required, mainly because discussions were in train between British Coal and the CEGB about the amount of coal to be supplied during the current financial year. Your officials have been kept in touch with the situation as it has developed.

The two industries have now reached a common view of coal supplies for 1987/88, which is reflected in their current financial projections for the year. On this basis, British Coal forecast an external financing requirement of £842m. I attach a full reconciliation with the present EFL of £727m. You will see that the increase is mainly attributable to more difficult market conditions (£320m) and to the higher restructuring cost associated with a faster manpower rundown than was assumed in last year's IFR (£90m). A number of other items add a further £77m, making a gross increase in the EFR of £487m.

The Corporation have continued to make stringent reductions in their costs (£116m), which together with a reduced contingency allowance (£98m), the contributions holiday in the Staff Superannuation Scheme (£48m) and other miscellaneous items (£60m), makes total savings of £372m. I do not think it would be realistic to expect British Coal to achieve greater cost savings than this in 1987/88; nor would it be sensible to look for any reduction in this year's capital expenditure: such reductions would jeopardise the cost savings needed for continuing improvement on revenue account.

There is one important uncertainty to which I must draw your attention. The figures assume that British Coal's new redundancy terms will result in a manpower rundown in line with their budget

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SECRETARY OF STATE FOR ENERGY

(total rundown 10,000; industrial redundancies 6,300). If the new terms should result in higher redundancies, British Coal's cash needs would be correspondingly increased: it is estimated that each additional 1000 redundancies would increase the EFR by £18m. Given British Coal's current and prospective market difficulties, I am sure that it would be wrong to hamper essential reductions in labour costs. My officials are, of course, monitoring the situation carefully with British Coal and will keep yours fully informed.

I therefore propose an increase in British Coal's EFL for 1987/88 to £842m. If you agree, I suggest that I should announce this as soon as possible.

Yours Ever,

Cecil

CECIL PARKINSON

RECONCILIATION BETWEEN EXISTING £727M EFL AND PROPOSED NEW £842M EFL

	£m	£m
Existing EFL		727
Deteriorations		
Lower proceeds per tonne sold	320	
Higher restructuring cost (net of higher stage funding creditor)	90	
Extra coal supplied to CEGB under deferred payment arrangements	22	
Increase in interest	21	
Payment of wages arrears carried over from 1986/87	18	
Support for boiler conversion project	8	
Early repayment of ECSC loans	7	
Others	1	

		487
Improvements		
Cost reductions	166	
Staff superannuation contributions holiday	48	
Reduced contingency	98	
Spreading of release of strike provision for MPS deficiency	24	
Increase in sale of fixed assets	14	
Reduction in stock of stores	22	

		372

Proposed new EFL		842
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