PREM 19/1412

PART 3

2/14 SECRET

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The Future and Structure of British Airways

The Price Waterhouse Report

CAA Review

AEROSPACE

Pt 1: MARCH 1982

Pt 3: OCTOBER 1984

PREM 19/1412

Referred to	Date	Referred to	Date	Referred to	Date	Referred to	Date
3.10.84		8.3.85					
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1.11.84		18.3.85					
8.11.84		26.3.85					
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PART 3 ends:-

E (A) (85) 8th Mtg LCA 3/4/85

PART 4 begins:-

Transport to HMC 3/5/85

TO BE RETAINED AS TOP ENCLOSURE

Cabinet / Cabinet Committee Documents

Reference	Date
C(84) 27	01/10/1984
CC(84) 32nd Meeting, item 6	04/10/1984
CC(84) 32nd Meeting, item 6 Limited Circulation Anx	04/10/1984
CC(84) 35th Meeting, item 2	01/11/1984
CC(84) 40th Meeting, item 3	06/12/1984
CC(84) 41st Meeting, item 1	13/12/1984
MISC 112(85) 2	15/01/1985
MISC 112(85) 3	15/01/1985
MISC 112(85) 4	15/01/1985
MISC 112(85) 5	16/01/1985
MISC 112(85) 6	18/01/1985
MISC 112(85) 2nd Meeting	06/03/1985
E(A)(85) 17	27/03/1985
CC(84) 12th Meeting, item 5	28/03/1985
E(A)(85) 18	28/03/1985
E(A)(85) 19	28/03/1985
E(A)(85) 20	29/03/1985
E(A)(85) 22	01/04/1985
E(A)(85) 8th Meeting, Limited Circulation Annex	03/04/1985

The documents listed above, which were enclosed on this file, have been removed and destroyed. Such documents are the responsibility of the Cabinet Office. When released they are available in the appropriate **CAB** (CABINET OFFICE) CLASSES

Signed J. Gray Date 14/11/2013

PREM Records Team

CONFIDENTIAL

P.01527

PRIME MINISTER

Airports Policy
E(A)(85)17, 18, 19, 20 and 22.

The Sub-Committee will be considering a broad range of issues which fall under the general heading of Airports Policy:

A (i) Airport development in South East England (covered in the Transport Secretary's paper E(A)(85)18, and the Minister for Housing and Construction's paper B E(A)(85)22);

(ii) policy on airports in the Scottish Lowlands (which is the subject of the Transport Secretary's paper C E(A)(85)17); and

(iii) the structure and ownership of airports in Britain (this is the subject of the Transport Secretary's paper D E(A)(85)19 and the Financial Secretary to the E Treasury's paper E(A)(85)20).

BACKGROUND

2. Far-reaching decisions are required on airport development in South East England, following the publication of the Inspector's report on proposals for the development of Stansted and for a fifth terminal at Heathrow. The question of the provision of adequate airport capacity in South East England has been a matter of great political controversy for 20 years, and this remains the situation. Objectors on environmental grounds to the development of Stansted as the third London airport have made common cause with supporters of airport development in the regions,

notably Manchester. The political and Parliamentary aspects of these decisions were the subject of your preliminary meeting on 27 March with the Transport Secretary, the Lord Privy Seal, the Chief Whip and the Minister for Housing and Construction; the outcome of that meeting was reported in your Private Secretary's letter of 27 March to Mr Ridley's Private Secretary.

3. The problem in Lowland Scotland is the opposite of that in South East England: there is surplus airport capacity, and Prestwick, which is designated as the 'gateway' airport for international traffic is under-used and losing money. The question is whether this policy should be maintained, or whether airlines should be permitted to move their flights to Glasgow and Edinburgh.

4. On the structure and ownership of airports, the 1983 Manifesto stated the Government's aim that as many airports as possible should become private sector companies. The question arises, therefore, how this policy should be applied to the major airports under the control of the British Airports Authority (BAA) and also to the regional airports which are generally owned by local authorities. Because of the natural monopoly position of major airports, and of international obligations in the civil aviation field, legislation to privatise BAA airports is likely to require to be accompanied by further provisions to establish a new framework of statutory regulation of airports.

MAIN ISSUES

5. The following are the main issues before the Sub-Committee:

(i) should planning permission be given for the development of Stansted as the third London airport, up to a limit of 15 million passengers per annum (MPPA), with the implication that a further major public enquiry would be required before the volume of passanger traffic was

increased to the maximum capable of being accommodated by the runway, ie 25 MPPA?

(ii) Should the previously intended Air Traffic Movement (ATM) limit at Heathrow of 275,000 a year be increased on the opening of the Fourth Terminal to a new level which would not imply any effective constraint on the use of the runways? Should any decision* on a fifth terminal at Heathrow be postponed until the future shape of air traffic there is clear, with studies being undertaken in the meanwhile of possible improvements in surface access to the airport, and of the implications of moving the Perry Oaks Sludge Works (on which site a fifth terminal would need to be built)?

*Formally, of course, the immediate decision is to reject the Fifth Terminal planning application.

(iii) Should Luton Borough Council be encouraged to propose a limited development of Luton Airport?

(iv) Should Prestwick be maintained as the 'gateway' airport for international flights to Scotland?

(v) Should the BAA be privatised as soon as possible? If so, should this be as a single unit or with the London and Scottish airports being privatised as separate groups?

(vi) Should all major airports be established as separate Companies Act Companies?

(vii) In the event of privatisation, should legislation be enacted to impose a new statutory control of access to airports, airport charges and investment in airport capacity?

(viii) When should the Government's decisions be published and debated by the House of Commons?

(ix) Should there be new primary legislation in the 1985-86 Session covering statutory control on ATM limits, BAA privatisation and the regulatory framework?

Stansted

6. The opening next year of the Fourth Terminal at Heathrow, and the Second Terminal at Gatwick, should provide enough passenger handling capacity to meet London's needs until about 1990. But further capacity will almost certainly be needed shortly thereafter, with availability of runways rather than passenger terminals the operative constraint. The only available runway is that at Stansted, and work will need to start in the near future if the necessary terminal facilities and transport infrastructure are to be provided within the necessary timescale. Mr Ridley's proposal is that planning permission should be given for development of Stansted up to 15 MPPA, with facilities for 7 MPPA to be constructed as the first stage and the Government undertaking not to increase the ATM limit above that consistent with 7 MPPA without the agreement of Parliament. His intention in limiting the planning permission to 15 MPPA, and in providing Parliamentary safeguards within that figure, is to reassure the Northern lobby that there will be sufficient scope for the development of Manchester. Further inducements would be given to the Northern lobby through action to boost international traffic at Manchester, and to encourage further development of the airport facilities.

Heathrow

7. The Inspector's report assumed a continuing trend towards higher numbers of passengers per aircraft, which might eventually justify the construction of a Fifith Terminal to serve the two present runways. The development of feeder services in smaller aircraft seems likely in practice to restrict the average number of passengers per aircraft, with the implication that runway rather than terminal capacity will prove the operative constraint at Heathrow. On this basis the first task is to ensure that the fullest possible use is made of the present runway and terminal facilities; a decision can be taken later on the construction of a Fifth Terminal, if the shape of passenger traffic turns out to warrant this. Meanwhile the ATM limit of 275,000 a year

contemplated by Sir John Nott when he gave planning permission for the Fourth Terminal will need to be increased substantially, so that it does not serve as a constraint on the use of the runways. There is likely to be some local political opposition to this, but the lower noise levels on modern aircraft should go some way to allaying this concern. Contrary to the Inspector's recommendation, Mr Ridley does not propose to commit the Government to a ban on night flying.

Luton

8. More intensive use of Heathrow, together with the Development at Stansted, should provide the bulk of the required additional capacity for the early 1990s. However, Mr Ridley proposes supplementing the Inspector's recommendations by encouraging the Luton Borough Council to apply for planning permission to increase the annual throughput from 3½ MPPA to 5 MPPA or more. Luton would continue to concentrate on charter rather than scheduled services.

Future of Prestwick

9. This is an essentially political question, which illustrates the particular economic constraints under which airports have to operate. A small improvement in traffic would make Prestwick profitable; but there is plenty of spare capacity at Glasgow and Edinburgh, which could easily absorb the traffic which now uses Prestwick. Since the airlines would rather fly to Glasgow and Edinburgh, the normal prescription would be to save the costs of operating Prestwick, and increase profit levels at Glasgow and Edinburgh. However, because international obligations require airport charges to be related to costs (and profits from duty-free etc activities to be applied to reducing charges), all the gains from closing Prestwick would accrue to the airlines and their passengers, rather than to the airport proprietors. Meanwhile closure of Prestwick would

mean the direct loss of about 1,000 jobs there (partly offset by higher employment at Glasgow and Edinburgh), and would put at risk the continued operation of the British Aerospace (BAe) plant there, which is engaged on the Jetstream and would have undertaken part of the work on the RAF Basic Trainer, had BAe secured that contract.

Privatisation of BAA

10. The Financial Secretary (in his paper E(A)(85)20) urges that the Government should proceed as quickly as possible with the privatisation of BAA as a whole, which would raise £500 to £600 million. Mr Ridley recommends that each major airport should be turned into a Companies Act Company, and that BAA should be split into two major groups, one incorporating the London airports and the other those in the Scottish Lowlands (there is then a subsidiary question whether Aberdeen should be in the Scottish Lowlands group, as Mr Younger prefers, or whether it should be privatised separately, as Mr Ridley recommends). These steps would clear the way for privatisation, but the decision to privatise need not be taken yet. The principal advantage of privatisation is the substantial cash flow to the Government; as the case of Prestwick illustrates, and as Mr Ridley recognises, the practical advantages of privatisation in terms of the spur it offers to efficiency, economy and profitability apply with much less than their usual force to the case of airports. BAA has a good record in meeting financial targets, and many of the normal benefits of privatisation have already been secured by franchising much of the activity which goes on at BAA airports. The increase in managerial independence following privatisation would be relatively modest; the level of charges would continue to be tightly constrained by international civil aviation obligations, while the Government would inevitably continue to have the last word in major investment decisions.

Splitting the BAA

11. Mr Ridley considers that the BAA is too large and dominant, and that there would be greater scope for independent and competitive management expertise if it were broken down into its component parts. However, Mr Ridley also recognises that the three London airports have to be operated as a group, with charges set on a coordinated basis and with some central authority to determine which service uses which airport. The same applies to Glasgow Edinburgh and Prestwick. Mr Ridley can only suggest, therefore, that the BAA should be divided into two parts - and this, as Mr Moore points out, leaves the London BAA group still overwhelmingly dominant in terms of total UK civil air traffic. Moreover splitting the BAA would mean that the Scottish group could not be privatised until after the next election, whereas privatisation of BAA as a whole (or of the London group only) would be feasible - following the enactment of the necessary legislation - in the Spring of 1987. No assessment is provided in the papers whether the Net Present Value of the privatisation receipts would be greater if BAA were privatised as a whole or in two parts.

Airports as Companies Act Companies

12. Mr Ridley's proposal that each airport should be established as a Companies Act Company is intended to provide for equal conditions of competition between airports, and to facilitate the privatisation of airports in municipal hands. Although this step should make it easier to compare the performance of airports, the international constraints on their operation and the need to run the London and Scottish Lowlands airports as groups would appear to reduce the advantages of this. It would undoubtedly be helpful to provide for the attraction of private capital into municipal airports, but where airports are in a position to contribute cash flow towards the maintenance of other municipal services, the effect of imposing a liability to corporation tax (from which local authorities are exempt, but which would apply

automatically once municipal airports had been constituted as Companies Act Companies) would be a further factor to be taken into account in the Government's overall review of local authority finance.

Regulatory regime

13. If the Government decide to go ahead with privatisation, new regulatory powers will be needed, to be exercised by the Civil Aviation Authority (CAA) and the Transport Secretary. The Department of Transport's first shot at what would be involved in this is at Annex D to E(A)(85)19. Further work is needed to establish more precisely the form and extent of regulations; but it seems clear that the CAA or some comparable body would need to retain power to ensure airlines' access on equitable terms to the various airports, to control charges consistently with international obligations and with the for airports to be operated efficiently, and to ensure that airport capacity is available where and when needed. Mr Ridley envisages that this last responsibility would be discharged by adjusting permitted levels of charges so as to give airport proprietors the necessary incentives to undertake investments.

Content and timing of legislation

14. Depending on the Sub-Committee's decisions, new primary legislation would be envisaged in the 1985-86 Session covering

(i) control, by Order subject to Parliamentary control, of Air Traffic Movements (ATMs) at each airport (the Bill before the current Session which would achieve this would be withdrawn);

(ii) privatisation of BAA;

(iii) conversion of all major airports into Companies Act Companies; and

(iv) the imposition of a new regulatory regime on airport operations.

In considering the Legislative Programme for the next Session, the Queen's Speeches and Future Legislation Committee (QL) envisaged that a Bill would be needed covering (ii) and (iii) above, but not (i) and (iv). If all these elements are to be covered, including regulation which seems likely to be of considerable complexity, then the business managers and the Parliamentary draftsmen will be facing a very substantial task. QL may therefore need to consider what other legislation might be dropped from next Session's Programme, in order to make room for a very considerably expanded Civil Aviation Bill.

Timing of an announcement

15. The Inspector's report was published last December, and a preliminary debate in the House of Commons was held in mid-January. The Government will be under increasing pressure to announce their intentions; and the sooner an announcement is made, the sooner the preparation of the necessary legislation can get under way. Mr Ridley is working towards publication of a White Paper in mid-May, which would cover all aspects of the Government's airport policy - the development of Stansted, privatisation of BAA and establishment of major airports as Companies Act Companies, and the regulatory regime. The formal decision letters arising from the Stansted and Heathrow planning applications would be issued at the same time. The way would then be open for a Parliamentary Debate on the White Paper - on a substantive motion - to be held just before the Whitsun Recess. This is an ambitious timetable, which could only be achieved if the Sub-Committee reaches clear decisions on all the outstanding issues.

HANDLING

16. I suggest that the discussion should be divided into three parts: the Development of Stansted and Heathrow; the Future of Prestwick; and the Privatisation/Regulation issues. (It may be helpful to the other Ministers if you make this clear at the outset.) The Transport Secretary will wish to introduce his paper on airport development in the South East, and the Minister for Housing and Construction (who is in effect jointly responsible for the planning decision) will wish to add his comments, not least in relation to the problems of moving the Perry Oaks Sludge - Works (which are the subject of his separate paper (E(A)(85)22). The economic case for Mr Ridley's proposals appears to be well established, but a number of other Ministers may wish to comment from a political or regional policy standpoint. On Prestwick, the Transport Secretary and the Secretary of State for Scotland will wish to state their positions, as will the Chief Secretary to the Treasury. On privatisation, the Transport Secretary will again wish to introduce the discussion, and the Financial Secretary to the Treasury will wish to comment. The issues here are all inter-related, but it may be convenient to consider first whether or not to go ahead quickly with the privatisation of BAA; then to consider whether it should be divided into two groups (and whether or not Aberdeen should be included in the Scottish group); then to consider whether each major airport should be transformed into a Companies Act Company; and finally to consider the nature and extent of the regulatory regime required in the event of privatisation. You will also wish to have a discussion of the Parliamentary and legislative implications of the Sub-Committee's decisions.

CONCLUSIONS

17. You will wish to record conclusions on the following matters:

(i) the Development of Stansted. The decision will need to cover the passenger volume to be covered by the

planning permission, and the arrangements for control within this limit through statutory controls on ATMs;

(ii) the increase in the previously announced ATM limit at Heathrow, when Terminal Four opens, to a level which will not constrain the use of the runways. The decision will also need to cover what is to be said about the possibility of moving the Perry Oaks Sludge Works;

(iii) the Development of Luton;

(iv) whether or not Prestwick should be closed within the next few years;

(v) whether BAA should be privatised at the earliest opportunity;

(vi) whether BAA should be split into two groups, and whether or not Aberdeen should be retained within the Scottish group;

(vii) whether or not all major airports should be established as Companies Act Companies;

(viii) the regulatory regime required in the event of airports privatisation;

(ix) the content and timing of legislation to give effect to the Sub-Committee's decisions, and its implications for the Government's Legislative Programme in the next Session;

(x) arrangements for the announcement of the Government's policy on airports, and for it to be debated in the House of Commons.

PLG

P L GREGSON
Cabinet Office
2 April 1985

CONFIDENTIAL

hle BEMAKY.

b/R. Wiggins, Cab. Off.

10 DOWNING STREET

From the Private Secretary

2 April 1985

FALKLANDS TROOPING CONTRACT

The Prime Miister has considered the Defence Secretary's minute of 29 March and the Transport Secretary's minute of 1 April about the Falklands Trooping Contract. She considers that we gave an undertaking to British Airways which we must honour but should discharge it in the way which least affects RAF morale and efficiency. She notes from the Transport Secretary's minute that British Airways would be prepared to accept a contract for six months only and at a reduced price. She concludes that the right course is to accept this.

I am copying this letter to the Private Secretaries to the Transport Secretary, the Chancellor of the Exchequer, the Lord Privy Seal, the Secretary of State for Trade and Industry and to Sir Robert Armstrong.

(C.D. Powell)

Richard Mottram, Esq.,
Ministry of Defence

CONFIDENTIAL

PRIME MINISTER

FALKLANDS TROOPING CONTRACT

Michael Heseltine has minuted you about the difficulty which has arisen over the contract which, with the Cabinet's agreement, I told Lord King the MOD would place with British Airways; this was crucial to securing his acquiescence in our proposals for route swaps between BA and British Caledonian.

The previous correspondence between us, of which you have had copies, record the subsequent train of events, and I need not repeat it again. The simple issue is that British Airways were promised a contract to carry servicemen to and from the Falklands.

That was important to them because it helped to offset the work and revenue they lost from giving up profitable routes to Saudi Arabia in exchange for BCal's unprofitable services to South America. In their press release about the exchanges BA announced that they were going to get the Falklands contract.

In one respect Michael and I both misunderstood BA's intentions. The Tristars they wanted to lease from the RAF were not for the Falklands contract, although we thought they were. As soon as this had been clarified I made clear to BA that they were asking for the impossible. That took away a significant part of the deal they thought they were getting. Further, BA had asked for a three year contract, but accepted that 12 months might be all they could expect.

BA then made it clear that the use of a 747 for the Falklands task was more economical than using the smaller Tristars. The RAF's proposal to fly the service themselves emerged later.

The issue is not whether the RAF, having subsequently found a cheaper way of doing the job, should now be allowed to do so; but whether the Government, having given certain assurances in order to bring to a successful conclusion the extremely difficult and protracted negotiations I undertook with BA and BCal, should then go back on what it offered. To do so would not simply make the Government's word less credible in the eyes of Lord King and his employees: it will also make it much more difficult to insist on what we must tell BA about the balance sheet we present at privatisation. They too have a problem - they announced to their staff and the world that they were getting the contract, and would be seen to have been wrong.

I think it is vital that we find a solution which is honourable for all those concerned. To that end British Airways are prepared to reduce the price of a 12 month contract from £18.6 million to £17 million. As an alternative they have already indicated to the MOD that they would be prepared to accept a contract for 6 months only, at a price of £10 million. (The price cannot be reduced pro rata with time because there are substantial front-end costs which do not vary with the period of the contract.)

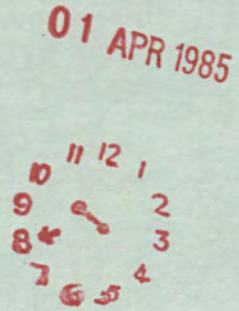
I urge you strongly that BA should be given a contract on one or other of these two bases.

Copies of this minute go to the Chancellor of the Exchequer, Secretary of State for Defence, Lord Privy Seal, Secretary of State for Trade and Industry and to Sir Robert Armstrong.

NR

NICHOLAS RIDLEY

1 April 1985


01 APR 1985

(1)

10 DOWNING STREET

Prime Minister

Falklands Trooping Contract

The Defence Secretary & the Transport Secretary are still completely at loggerheads: please see attached minutes.

Defence Secretary says giving BA the contract will cost more and demoralise the RAF, who would have nothing for their Tristars to do.

Transport Secretary says there is a debt of honour to BA; & they are prepared to

reduce the price they quote.

Can still have to arbitrate.

Agree to give the contract to BA for six months, to pay the debt? It's not long enough to cause the RAF a severe morale problem, or MOD a major budgetary one.

CDP 1/4

CCNO

MO 26/8/1

PRIME MINISTER

FALKLANDS TROOPING CONTRACT

You will have seen the exchanges of letters between Nicholas Ridley and myself over a Falklands trooping contract following the official opening of Mount Pleasant Airport in mid-May.

2. The point at issue relates neither to the longer term trooping service which will be by RAF-operated Tristars nor to the proving and inaugural flights which will be made by RAF Tristars with support from British Airways (BA). It is a short term problem covering a period, at the outside, of 12 months from the date of the Airport opening. Nor is there any dispute between us that British Airways were offered a trooping contract: the terms which I agreed, at the request of the Department of Transport, are set out in my letter to Nicholas Ridley of 18th March. BA no longer want to proceed on that basis; and the contract they now want is not the most efficient way of meeting the defence requirement. The question is whether the Government's commitment should be re-interpreted in the way that now best suits BA but which involves a cost to the defence budget and a significant risk of public criticism.

3. BA have offered a 747 contract for a year, or perhaps something shorter. This is certainly in line with the tenders that were under discussion at an earlier stage last summer; but it is not what they were offered following the Cabinet's decision. The RAF can themselves perform the task with the support of a contractor.

BA say they cannot provide contractor support but there are two other contractors who can do the job. An RAF Tristar service with contractor support would have a total cost up to £9M less than BA would charge for a 12 month contract with a 747. If we give BA the contract we shall have nothing for the RAF Tristars to do and will effectively have to ground them and their crews: the effects on RAF morale, when they know they can do the job more cheaply, are obvious. The grounding would inevitably become known and would have to be defended. This would not be easy.

4. We have also to consider the impact on BA. They will of course be disappointed but my own impression is that they will accept that circumstances have changed. The Chief Executive of BA has made it clear that, whatever the outcome on the contract, BA's good relationship with the Royal Air Force will not be affected.

5. This is not an easy decision. On balance, my own view is that I should tell BA that my Ministry does not require their 747, and that we should instead proceed with the RAF option with contractor support. I should be grateful to know that you are content.

6. I am copying this minute as in the previous correspondence.

Ramsbotham (approved by the Defence Secretary & signed in his absence)

Ministry of Defence
29th March 1985

AEROSPACE Pt 3

FUTURE

For E(A) Wed.

CONFIDENTIAL

PRIME MINISTER

29 March 1985

AIRPORTS - PRESTWICK, PRIVATISATION, WHITE PAPER

Nicholas Ridley wants E(A)'s endorsement for leaving a loss-making Prestwick Airport with BAA until after privatisation (1989); then its future can be decided on commercial grounds. George Younger supports this, as it avoids the political problems. The Treasury, claiming to champion airlines and consumers, would like to close Prestwick now.

Is Prestwick a problem or an opportunity? Prestwick's early closure would increase the sale value of BAA's Scottish airports, but the gain will be largely offset by the closure costs. Landing charges are less than 5% of the total cost of air travel. So any cost saving benefit to passengers would be tiny. There may be an economic case for closure, but the politics are difficult.

We would rather consider Prestwick through opportunistic business eyes. Unlike the London airports system (85% of BAA's assets) which is a safe, mature business suitable for the shareholding public, the Scottish airports offer more scope for imaginative, and perhaps risky, development. Suppose they were sold to an entrepreneurial group of business interests headed by someone like Nigel Broakes. The North Sea service and supply industry, Silicon Glen, tourism, Scotland's financial services, and the up-market Scottish craft industries all provide exciting business opportunities. So

too does golf, often interwoven with business. One only has to visit Gleneagles to see the yen and dollar earning potential of prestigious Scottish golf courses.

Seen in this context, Prestwick could look considerably more interesting than a loss-making conventional airport, at an awkward location. What about its free port? What about its capacity to handle long-haul intercontinental flights - unlike Glasgow and Edinburgh?

Conclusions

You could argue on Agenda Item 3.

1. Now that we have decided to privatise BAA's Scottish airports, we should not pre-empt the judgement of enterprising business interests for the future of Prestwick.

2. As there is an outside chance that an entrepreneur could do something with the Scottish airports, there is all the more reason to sell them separately from the London group.

Also, the White Paper should concentrate on selling the case for London (particularly Stansted) expansion and privatisation, and should not be cluttered with too many side issues which merely serve to increase the number of lobbies against the policy.

JOHN WYBREW

(2)

CC

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

Prime Minister

CDP 2073

Andrew Turnbull Esq
Private Secretary
10 Downing Street
LONDON SW1

28th March 1985

Dear Andrew,

LAKER: ATTEMPTED SETTLEMENT

In view of the Prime Minister's absence over Easter, Mr Ridley thought that we should report now on the current state of play in the settlement negotiations.

As you will know from Washington telno 848 of 8 March, Exim agreed to compromise their $65 million claim at $20 million. Of this, £8m would be in cash; the other £12m is the estimated present value of an increase in BA's interest payments on outstanding loans. (Given the lack of merit in the charge that the airlines conspired to bring down Laker, and in the Exim claim for interest, this was in Mr Ridley's view hardly generous, nor was there evidence that Administration intervention was conducted with such conviction as to have moved the Exim Chairman).

But as we anticipated, it is proving difficult to contain the repercussions of the deal extracted by Eximbank. The BA negotiators have had some success with most of the major creditors, but not with Airbus, who are taking the position that they want the same amount as Eximbank ($20 million). A critical meeting between the negotiators and the Chairman of Airbus is to take place at the end of this week (March 29). Mr Tebbit's officials will be emphasising to Airbus at a meeting on Thursday (March 28) the importance of a settlement for the aerospace industry as a whole and for Airbus in particular. There seems little doubt that if Airbus continued to hold out for parity of treatment with Eximbank the settlement would fall apart: the other major creditors would hardly accept exceptional treatment for both Eximbank and Airbus, and if all were treated alike the total cost of a settlement would rise enormously.

Other potential problems cannot yet be finally resolved (in particular Sir Freddie Laker and his lawyers) but the feeling is that the prospects for a settlement remain good if Airbus can be persuaded to settle for the $¼ million which they had accepted at an earlier stage.

As regards the timescale, the stay on discovery enforcement agreed by the US court expires on April 8. The liquidator has again indicated that he will oppose any further stay. If a settlement is not reached and he does not back off therefore, we could find ourselves in a conflict between the US Court and our PTI Act Order. On the other hand if a settlement is reached in the Laker liquidator's case, the prospects for going on to settle the class actions look reasonably encouraging; tentative approaches to the plaintiffs have shown that they are willing to dispose of these cases by settlement.

I am copying this letter to Peter Ricketts (FCO), Rachel Lomax (Treasury), Callum McCarthy (Department of Trade and Industry), Helen Goodman (Financial Secretary's office), Henry Steel (Law Officer's Department) and Richard Hatfield (Cabinet Office).

Yours,

Richard.

R A ALLAN
Private Secretary

CNO

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

The Rt Hon Michael Heseltine MP
Secretary of State for Defence
Ministry of Defence
Main Building
Whitehall
LONDON SW1A 2HB

26 March 1985

Dear Michael

FALKLAND ISLANDS TROOPING CONTRACT

I am afraid that I cannot accept the view expressed in your letter of 18 March that there is no effective difference between your leasing two Tristars to British Airways to enable them to undertake trooping flights for you - which is what you agreed to do last October - and your present proposal that BA should merely have a contract for some ground support while the RAF fly their Tristars themselves. There is a great deal between them in the amount of work and revenue which they would provide for British Airways, and it was your assurance to the Cabinet that that work would be forthcoming which enabled me to persuade Lord King to give up his claim to operate to Atlanta.

I do not dissent that when we agreed on this, we both believed that BA wanted the Tristars for the Falklands contract. As soon as it became clear that they wanted them for other work my Department persuaded BA that they could not expect the RAF to lease aircraft to them on a long term basis for commercial operations and they reluctantly sought these aircraft elsewhere. I have recorded that in my earlier letters. It became clear at the first meeting officials of our two

Departments had with British Airways on 19 October to discuss the contract, that BA were thinking that a 747 service (for which they had already tendered) would be a more efficient way of meeting your Falklands requirements than the use of Tristars, and they confirmed that a few days later. It was welcomed by the RAF because it would mean fewer movements at the new Falklands airport when it had just opened and some construction work was still being completed.

The proposal that the RAF should run the operation themselves, with only modest assistance from British Airways, emerged subsequently. It was certainly not the basis which you and I had discussed in relation to the CAA review, and it does not represent a satisfactory discharge of the commitment you gave me, and which I passed on to Lord King.

Agreements of that kind cannot be set aside simply because after they have been made someone has come up with a different way of meeting the requirement. I understand that British Airways are unable to give the RAF Tristars the support that they would need and without it the RAF may find it difficult to operate to the Falklands when the airport opens. BA have now been waiting nearly seven months for the contract they were promised. They have kept the 747 capacity available in the expectation of receiving it, but they cannot afford to do so much longer. You originally offered a three year contract - as you say - and that was subject to review after one year. I believe that BA would now settle for something slightly shorter than a year, but long enough to allow them time to find ways of using the aircraft subsequently.

They already feel that we have let them down over the leasing of the Tristars, despite the explanations we have given them. If they end up getting nothing at all, it will undoubtedly sour relations between HMG and Lord King, and make my position particularly difficult in negotiations with the airline over their capital structure for privatisation.

So I must ask you to reconsider your position again urgently.

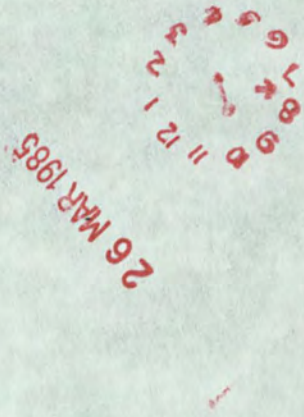
I am copying this letter as before to the Prime Minister, Nigel Lawson, Norman Tebbit, John Biffen and Sir Robert Armstrong.

Yours ever
Nicholas

NICHOLAS RIDLEY

AEROSPACE

FUTURE JOBAPTS



CDP 27/3

10 DOWNING STREET

Prime Minister

BA Trooping Contract for the Falklands

You saw some of the earlier papers on this, and should now see this further exchange between Defence & Transport.

You may in the end have to intervene: but I think you can let it go another round yet.

CDP 26/3

CC(N)

MINISTRY OF DEFENCE WHITEHALL LONDON SW1A 2HB

TELEPHONE 01-218 9000
DIRECT DIALLING 01-218 2111/3

MO 26/8/1

18th March 1985

Thank you for your letter of 15th March. Following our agreement last October, I thought it best to get those concerned here to sort out a mutually acceptable contract with British Airways, rather than to try to tie up all the details by correspondence at our level; and that is why I have not responded formally to your earlier letters. Our officials have of course been fully in touch from the outset. The matter is - regrettably - more complicated than your letter implies and it may be helpful to our colleagues if I set out the issues in full.

My Department has always intended to undertake in the longer term the air movement of passengers and priority freight to Mount Pleasant Airfield (MPA) using RAF Tristar 500s after their conversion by Marshall of Cambridge (Engineering) Ltd into tanker aircraft. Their primary role is to meet the surge in the requirement for air-to-air refuelling in war; but they will retain a major passenger and freight-carrying capability so that they can be used cost effectively in peacetime as part of the air transport force.

Early last year a possible gap was foreseen in 1985 between the opening of the MPA and the return following conversion of Tristars from Marshalls, when there might be no RAF wide-bodied transport aircraft available. The unknown factor was the timetable

The Rt Hon Nicholas Ridley MP

for the purchase of more Tristar 500s from Pam-Am. My officials sought tenders from civil operators to cover this gap, without commitment to award a contract. BA submitted a tender in July for a one-year B747 service at a cost to MOD of £28M, the aircraft to be specially leased; they also submitted a lower tender, but for an unacceptable route via the South American mainland, using their shorter-range Tristar 200s.

This was the position when the Cabinet were considering routes in October last. I was advised that British Airways wanted a trooping contract and to lease from the MOD two Tristars for the purpose. I offered a three year contract with a built-in one year break point and the lease of two ex-Pan Am Tristar 500s which my Ministry were about to purchase. This was my offer and I stand by my commitment to it.

When, however, officials subsequently met to finalise the details BA explained that they were still considering the respective merits of using the RAF Tristars or a B747 on the Falkland Islands military route; but then subsequently came down in favour of the latter and revealed that they also intended to fly the RAF Tristars on their new South American commercial routes. As you yourself recognised, such commercial flying was never part of the understanding we reached. It was no fault of my Department that a deal was not clinched on the basis agreed. Nor was there ever a commitment to award BA a one-year contract using a 747. This may be what suits them best but that is a different criterion to that of what was originally agreed between us.

My Department's strong preference is to fly RAF Tristars with the help of a contractor. This is cheaper and makes use of RAF assets which could otherwise have to be grounded. BA are the preferred contractor but if, as they now say, they are not interested, contract engineering support could be obtained elsewhere.

While we here could take the line that BA have chosen not to conclude a deal as originally agreed and therefore all bets are off, my own strong preference is for a mutually advantageous agreement. My officials have proposed a pooling of resources whereby the RAF Tristars would be operated between Brize Norton and the MPA for a year as a development of the present contract under which BA provide flight deck crews, cabin staff, engineering support and in-flight catering for two ex-BA Tristars. As part of the present deal, BA have also trained RAF flight deck crews who would need to share the flying task under the extension; but the number of hours to be flown would be doubled and the revised contract would be a substantial gain to BA. I find it difficult to believe that there is not the basis for a deal in an arrangement of this sort.

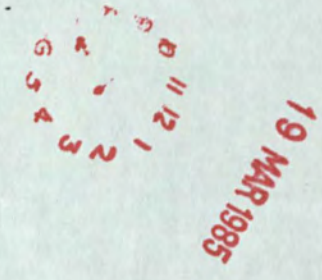
I remain then fully prepared to stand by my original offer to make available RAF Tristars as a basis for operating this route under the auspices of BA. I would very much like to see agreement reached in this matter. I have asked the Air Force Board Member concerned (Air Marshal Sir Michael Knight) to contact BA's Chief Executive to make one last effort. I urge you to use your influence with BA to seek an agreement which is both to their advantage and in the wider national interest.

I am copying this letter as yours.

Yours ever

Michael Heseltine

AEROSPACE : Future of British Airways:
Pt 3.



CF
11.30
Wed
27 Nov
CR
1913.

10 DOWNING STREET

Caroline.

We will need urgently a meeting on airports policy with S/Transport, Gow, LPS & Chief Whip on Monday or Tuesday next week - just possibly Wednesday. Its important enough to squeeze media interviews and cut hard for if necessary.

JR.

CC NO

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

Prime Minister (2)

To be aware.

AT
15/3

The Rt Hon Michael Heseltine MP
Secretary of State for Defence
Ministry of Defence
Main Building
Whitehall
LONDON SW1A 2HB

15 March 1985

Dear Michael

MT

FALKLAND ISLANDS TROOPING CONTRACT FOR BRITISH AIRWAYS

I have been most surprised and disappointed that I have still received no reply from you to my letters of 13 December and 6 February about this contract, about which British Airways ask us almost daily.

Perhaps I may remind you that when the Cabinet met on 4 October to discuss my proposals for the Government response to the Civil Aviation Authority's proposals on airline competition policy, you informed us that BA's tender for four trooping flights a week to the Falkland Islands had been the most advantageous, and that subject to final confirmation of the requirement, you had decided the contract should be awarded to BA.

The Cabinet therefore asked me to inform Lord King of your decision, and to seek to persuade him, in the light of that decision, to agree to an exchange of routes which did not include the route to Atlanta, which was proving the sticking point in final agreement with BA and BCal.

I am told that your Department are now reluctant to place that contract, because with hindsight they would now prefer to operate their own aircraft. However as a result of what you informed the Cabinet, British Airways have taken certain decisions, and they have a right to expect the Government to keep its part of the bargain which was authorised by Cabinet, and was struck with the airline. May I therefore please have your confirmation during the course of next week that you will be placing this contract without further delay.

I am copying this letter as before to the Prime Minister, Nigel Lawson, Norman Tebbit, John Biffen and Sir Robert Armstrong.

Yours ever

Nicholas

NICHOLAS RIDLEY

AEROSPACE

Future of BD

GRS 450
D E D U P

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CONFIDENTIAL
DESKBY 110830Z
FM WASHINGTON 090155Z MARCH 85
TO IMMEDIATE FCO
TELEGRAM NUMBER 648 OF 8 MARCH
LAKER SETTLEMENT

1. PARK (LINKLATER) AND MARSHALL (BA) REPORTED ON THIS AFTERNOON'S MEETING WITH EXIMBANK. THEY HAD SHAKEN HANDS ON THE FOLLOWING ARRANGEMENTS. EXIM WOULD RECEIVE EIGHT MILLION DOLLARS CASH PLUS A SUM AMOUNTING TO TWELVE MILLION DOLLARS PRESENT VALUE PRODUCED BY INTEREST RATE ADJUSTMENT. BA WOULD FOREGO THE RIGHT TO DRAW DOWN HALF OF THE OUTSTANDING 120 MILLION DOLLARS, LEAVING AN OUTSTANDING CREDIT OF 60 MILLION DOLLARS. ON THE BASIS OF EXIM'S VALUATION OF THE FOREGONE DRAW DOWN RIGHTS AT FIVE MILLION DOLLARS, THE TOTAL VALUE OF THE PACKAGE WAS 25 MILLION DOLLARS.

2. ON BA'S SIDE THE AGREEMENT WAS SUBJECT TO APPROVAL BY ITS BOARD, ITS SHAREHOLDER AND THE OTHER CREDITORS. ON EXIM'S SIDE THE AGREEMENT WAS SUBJECT TO APPROVAL BY ITS BOARD.

3. PARK AND MARSHALL THOUGHT THAT IT SHOULD BE POSSIBLE TO CONTROL THE KNOCK-ON EFFECTS ON THE OTHER CREDITORS, ALTHOUGH AIRBUS REMAINED A PARTICULAR PROBLEM. AS A NEXT STEP, MARSHALL WOULD BE CONTACTING AIRBUS AS SOON AS POSSIBLE IN ORDER TO ATTEMPT TO SECURE THEIR SUPPORT.

4. A FURTHER SOURCE OF CONCERN REMAINED BECKMAN (LIQUIDATOR'S ATTORNEY) TOGETHER WITH THE ANTI-TRUST LAWYERS WHOM HE HAD HIRED IN THE CASE, AND SIR FREDDIE LAKER. IF BOTH PARTIES WITHHELD THEIR AGREEMENT IN COMBINATION THERE COULD BE CONSIDERABLE DIFFICULTIES.

5. IN ANY EVENT BA AND EXIMBANK ARE NOW DRAWING UP A MEMORANDUM OF UNDERSTANDING EMBODYING THEIR AGREEMENT.

6. WE AGREED WITH MARSHALL AND PARK THAT THE PRESS LINE TO BE TAKEN FOR THE TIMEBEING WOULD BE THAT TALKS ARE CONTINUING AND PROGRESS IS BEING MADE. WE SHALL CONTINUE TO TAKE THE LINE THAT THE NEGOTIATIONS ARE BEING CONDUCTED BY BA TOGETHER WITH THE OTHER DEFENDANTS, AND REFER PRESS ENQUIRIES TO BA.

CONFIDENTIAL

17

7. FCO PLEASE PASS ADVANCE COPIES TO PS/SECRETARY OF STATE, PS/NO 10, PS/ SECRETARY OF STATE FOR TRADE AND INDUSTRY, PS/ATTORNEY GENERAL, PS/FINANCIAL SECRETARY, PS/SECRETARY OF STATE FOR TRANSPORT, KNIGHTON, HOLMES, FORTNAM (DTP), BRAITHWAITE, O'NEILL, GRAY (FCO), AUST (LEGAL ADVISERS, FCO), AYLING (SOLS, DTI), GARDINER (LAW OFFICERS' DEPT), HEALEY, RICKFORD (DTI), GREGSON (CABINET OFFICE), WILSON (TREASURY).

WRIGHT

(ADVANCED AS REQUESTED)

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HD/MAED
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PS
PS/MR PENTON
PS/PUS
MR BRAITHWAITE
MR O'NEILL

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FM WASHINGTON 090150Z

TO IMMEDIATE FCO

TELEGRAM NUMBER 847 OF 8 MARCH 1985

ADVANCE COPY

IMMEDIATE

LAKER CLASS ACTION SETTLEMENT

1. PARK (LINKLATERS) GAVE US AN ACCOUNT OF THEIR FIRST MEETING WITH COHEN (PLAINTIFF'S ATTORNEY) ON 7 MARCH. ALTHOUGH HE WAS OF COURSE VERY CAUTIOUS ABOUT DRAWING CONCLUSIONS FROM AN INITIAL EXPLORATORY MEETING, PARK SAID THAT COHEN'S APPROACH HAD BEEN PROMISING. HE HAD SEEMED GENERALLY IN FAVOUR OF A SETTLEMENT, PARTLY PERHAPS BECAUSE HE HAD RECENTLY BEEN APPOINTED COUNSEL IN THE BHOPAL CASE AND THUS HAD OTHER FISH TO FRY. COHEN WAS VERY CONSCIOUS THAT THE LARGE NUMBERS IN THE CLASS COULD MAKE THE CASE UNMANAGEABLE, AND HAD SEEMED WELL DISPOSED TOWARDS DEFINING THE CLASS NARROWLY SO AS TO RESTRICT THE NUMBERS. THIS WAS IN PRINCIPLE HELPFUL, BUT A NARROW DEFINITION OF THE CLASS COVERED BY THE SETTLEMENT COULD IMPLY A GREATER EXPOSURE TO FUTURE CLASS ACTION LAWSUITS, AND A BALANCE WOULD HAVE TO BE STRUCK.

2. THE MEETING WITH COHEN HAD CONFIRMED PARK IN HIS BELIEF THAT IT WAS NOW RIGHT TO PRESS AHEAD WITH THE CLASS ACTION SETTLEMENT WITHOUT NECESSARILY SETTLING THE LIQUIDATORS' ACTION FIRST. INDEED THE OPTIMUM RESULT MIGHT BE TO ANNOUNCE SETTLEMENT OF THE TWO TOGETHER. AS A FIRST STEP IN THE FURTHER PREPARATIONS FOR THE NEGOTIATIONS, WE HAVE ARRANGED A FURTHER MEETING BETWEEN PARK/BRISTER, JOELSON (HMG'S ATTORNEY) AND OURSELVES ON THE AFTERNOON OF 11 MARCH.

3. FCO PLEASE ADVANCE COPIES TO PS/SECRETARY OF STATE, PS/NO 10, PS/SECRETARY OF STATE FOR TRADE AND INDUSTRY, PS/ATTORNEY GENERAL, PS/FINANCIAL SECRETARY, PS/SECRETARY OF STATE FOR TRANSPORT, KNIGHTON, HOLMES, FORTNAM (DTP), BRAITHWAITE, O'NEILL, GRAY (FCO), AUST (LEGAL ADVISERS, FCO), AYLING (SOLS, DTI), GARDINER (LAW OFFICERS' DEPT), HEALEY, RICKFORD (DTI), GREGSON (CABINET OFFICE), WILSON (TREASURY).

WRIGHT

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GRS 1200

DEDIP
CONFIDENTIAL
DESKBY 070830Z
FM WASHINGTON 070715Z MARCH, 1985
TO IMMEDIATE F C O
TELEGRAM NUMBER 798 OF 7 MARCH.

Summary only.
I suggest
CDP

YOUR TELNO 408: LAKER

MT

SUMMARY

1. BA HAD TWO FURTHER MEETINGS WITH DRAPER AND ALBRIGHT TODAY. AT THE FIRST DRAPER CAME DOWN TO DOLLARS 28 MILLION (SPLITTING THE DIFFERENCE BETWEEN DOLLARS 33 MILLION AND WHAT HE SAID WAS BA'S POSITION, NAMELY DOLLARS 23 MILLION) OR BINDING MEDIATION ON THE BASIS OF SEALED BIDS FROM EACH PARTY TO A MEDIATOR. AT THE SECOND MEETING DRAPER SHOWED INTEREST IN A BA OFFER OF DOLLARS 25.5M INCLUDING DOLLARS 5M NON-DRAWDOWN. RESUMPTION OF DISCUSSION ON 8 MARCH.

DETAIL

2. BA MET DRAPER AFTER LUNCH. DRAPER REVEALED THAT HE HAD TALKED TO REGAN BUT DID NOT SAY WHEN. HE HAD ALSO TALKED TO WALLIS. NEITHER HAD GIVEN HIM ANY INDICATION THAT IN THE ADMINISTRATION'S VIEW THE MAXIMUM AMOUNT EXIMBANK COULD EXPECT TO OBTAIN WAS DOLLARS 20-22 MILLION. MOREOVER THE STATE DEPARTMENT HAD TOLD HIM THAT ACCORDING TO THE BRITISH EMBASSY (SIC), BA'S OFFER WAS DOLLARS 23 MILLION. HE THEREFORE PROPOSED TO SPLIT THE DIFFERENCE BETWEEN DOLLARS 33 MILLION (PARA 6 OF MY TELNO 783) AND DOLLARS 23 MILLION, PRODUCING DOLLARS 28 MILLION. ALTERNATIVELY WALLIS HAD SUGGESTED TO HIM THAT THE TWO PARTIES SHOULD AGREE ON A MEDIATOR. EACH PARTY WOULD GIVE THE MEDIATOR SEALED BIDS AND THE MEDIATOR, IN A BINDING DECISION, WOULD CHOOSE WHICHEVER BID WAS FURTHEST FROM EITHER PARTY'S POINT OF DEPARTURE (WHICH HE SPECIFIED AS DOLLARS 33 MILLION AND DOLLARS 23 MILLION). HE TURNED A DEAF EAR TO BA'S INSISTENCE THAT DOLLARS 23M WAS NOT THEIR POSITION AND THAT EXIMBANK COULD NOT LEGITIMATELY CLAIM INTEREST ARISING AFTER THE LIQUIDATION, SO THAT THE MAXIMUM POSSIBLE CLAIM WAS DOLLARS 21-22 MILLION. DRAPER INSISTED THAT THE ADMINISTRATION HAD CONVEYED NO SUCH MESSAGE TO HIM. BA AND EXIMBANK AGREED TO MEET AGAIN AT SIX IN THE EVENING.

3. MINISTER COMMERCIAL TELEPHONED THE STATE DEPARTMENT, GETTING MORRIS, TO CLEAR UP POSSIBLE STATE DEPARTMENT MISUNDERSTANDINGS AND HAVE THAT CLARIFICATION CONVEYED TO DRAPER. MORRIS SAID THAT HE WAS UNDER NO MISAPPREHENSION THAT BA WERE OFFERING DOLLARS 23 MILLION: HE HAD UNDERSTOOD PERFECTLY FROM YESTERDAYS CONVERSATION (PARA 9 OF MY TELNO 783) THAT BA'S OFFER WAS DOLLARS 18.2 MILLION: HE/WALLIS HAD CONVEYED THIS TO EXIMBANK. ALTHOUGH HE HAD UNDERSTOOD THAT BA WERE PREPARED TO TALK ABOUT BRIDGING THE GAP BETWEEN

/ DOLLARS

DOLLARS 18.2 MILLION AND DOLLARS 30 MILLION, HE HAD DELIBERATELY NOT CONVEYED THIS TO EXIMBANK. HE COMMENTED THAT DOLLARS 23 MILLION WAS IN ANY CASE A FIGURE WITHOUT ANY PARTICULAR MEANING IN THE CONTEXT OF BRIDGING A GAP BETWEEN DOLLARS 18.2 AND DOLLARS 30 MILLION. HE WAS UNABLE TO SUGGEST HOW DRAPER HAD GOT HOLD OF IT. MORRIS FURTHER SAID THAT, WHILE IT WAS TRUE THAT THE ADMINISTRATION HAD NEVER SUGGESTED ANY PARTICULAR FIGURE TO DRAPER AT WHICH HE SHOULD SETTLE, IT HAD BEEN MADE ABUNDANTLY AND STRONGLY CLEAR TO HIM BOTH THAT THE PRESIDENT WANTED A SETTLEMENT AND THAT IN US AS WELL AS JERSEY LAW, EXIMBANK WAS NOT ENTITLED TO POST LIQUIDATION INTEREST.

4. MORRIS ALSO SAID, ON THE MEDIATION POINT, THAT WALLIS HAD CONVEYED TO DRAPER THE TECHNIQUE SHULTZ HAD USED IN HIS DAYS AS A LABOUR MEDIATOR. THIS WAS INDEED A SEALED BID APPROACH WITH THE MEDIATOR'S DECISION BINDING, BUT THE GROUND RULES WERE AGREED BETWEEN THE TWO SIDES FIRST AND IT WAS NOT NECESSARY THAT THE MEDIATOR SHOULD ACCEPT THE BID OF THE PARTY WHICH HAD MOVED FURTHEST NUMERICALLY FROM ITS STARTING POSITION.

5. MINISTER COMMERCIAL ALSO SPOKE TO DAWSON, REGAN'S EXECUTIVE ASSISTANT IN THE WHITE HOUSE (WHO, WE HEARD FROM OTHER SOURCES, SPOKE TO ALBRIGHT THIS MORNING TO GIVE HIM AN ACCOUNT OF MY PHONE CALL TO REGAN). HE SAID THAT FOLLOWING MY TELEPHONE CONVERSATION WITH REGAN LAST NIGHT, THE TALKS NOW LOOKED AS IF THEY MIGHT BE HEADING FOR BREAKDOWN. DRAPER WAS SHOWING HIMSELF UNABLE OR UNWILLING TO RECOGNISE THAT BA COULD NOT POSSIBLY PAY EXIMBANK 100 PER CENT AND MORE OF THEIR MAXIMUM POSSIBLE ENTITLEMENT. AGREEMENT WITH EXIMBANK ON SUCH TERMS WOULD HAVE A MASSIVE ESCALATOR EFFECT AND DESTROY THE SETTLEMENT WITH THE OTHER PARTIES INVOLVED. DRAPER MIGHT OF COURSE MERELY BE NEGOTIATING TOUGHLY, BUT IF HE MEANT WHAT HE WAS SAYING (AND CROWE EXPLAINED WHAT THAT WAS) SUCCESS WAS IMPOSSIBLE. DAWSON SAID HE WOULD ''TAKE IT UP''
.

6. WHEN BA MET DRAPER AGAIN AT 6.00PM, DRAPER - AWKWARDLY BUT DELIBERATELY - SET ABOUT DISAVOWING THAT THE BRITISH EMBASSY HAD BEEN THE SOURCE OF THE ALLEGED DOLLARS 23M BA OFFER AND ALLUDED VAGUELY TO AMBASSADOR PRICE AS THE SOURCE. ON THE SUBSTANCE BA SAID THAT THEY WERE PREPARED TO GO UP TO DOLLARS 21M - 22M SUBJECT TO CLEARING WITH HMG AND OTHER CREDITORS AND DEFENDANTS. DRAPER INDICATED ACCEPTANCE OF DOLLARS 21M-22M PROVIDING THIS EXCLUDED NON-DRAWDOWN, ON THE BASIS THAT IT WAS VALUELESS. THIS HAD TO INCLUDE DOLLARS 8M OR WHATEVER LAKER RECEIVED IN CASH, THE BALANCE TO BE MADE UP IN INTEREST ADJUSTMENT. BA IMPLICITLY REJECTED THIS. MARSHALL MADE THE POINT THAT BA WERE CONSIDERING BUYING FURTHER 757S AGAINST THE DRAWDOWN, BUT THAT EXIMBANKS ATTITUDE MADE SUCH A PURCHASE DIFFICULT. HE OFFERED INSTEAD DOLLARS 25.5 INCLUDING DOLLARS 10M NON-DRAWDOWN. EXIMBANK REJECTED THIS. MARSHALL THEN SUGGESTED DOLLARS 25.5M, INCLUDING DOLLARS 5M NON-DRAWDOWN. EXIMBANK WERE INTERESTED ON THE BASIS

/ THAT

THAT THIS INCLUDED DOLLARS 8M, OR WHATEVER LAKER RECEIVED, CASH. BA MADE CLEAR THEIR BASIS, NAMELY CLEARANCE WITH HMG AND WITH OTHER CREDITORS FOR KNOCK-ON EFFECT. IT WAS AGREED TO DISCUSS FURTHER ON 8 MARCH AFTER FURTHER REFLECTION BY BA.

7. DRAPER IN THE COURSE OF THE DISCUSSION POINTEDLY ASSERTED THAT
A. NOBODY TOLD HIM WHAT TO DO ON FIGURES
B. AMBASSADOR PRICE IN PARTICULAR HAD NO AUTHORITY OVER HIM.

8. LIKEWISE - FOR WHAT IT IS WORTH - DURING THE DISCUSSION EXIMBANK VALUED HALF OF THE NON-DRAWDOWN AS DOLLARS 60M RATHER THAN DOLLARS 45M.

9. AFTER THE MEETING DRAPER PHONED MARSHALL BY PRE-ARRANGEMENT. HE SAID THAT EXIMBANK'S CALCULATION OF THE PRESENT VALUE OF THE INCREASED INTEREST ON BA LOANS WAS BASED ON EXIMBANK'S CURRENT COST OF LENDING AT 11.5 PERCENT. BA'S CALCULATION HAD BEEN BASED ON THEIR CURRENT LOAN RATE OF 9.25 PERCENT. EXIMBANK'S CALCULATION WOULD REQUIRE A CORRESPONDINGLY LARGER INCREASE IN INTEREST RATES TO ACHIEVE THE SAME PRESENT VALUE. MARSHALL SAID HE WAS RETURNING TO LONDON TONIGHT (WEDNESDAY) AND WOULD RETURN ON 8 MARCH. DRAPER SUGGESTED THAT HE AND MARSHALL COULD SETTLE THE MATTER BY TRANSATLANTIC TELEPHONE CONVERSATION. (PARK REGARDED THIS AS UNREALISTIC AND EXPECTS MARSHALL TO RETURN).

10. WE UNDERSTAND BA ARE CALCULATING HOW THEY COULD MAKE UP THE DOLLARS 20.5M (DOLLARS 25.5 LESS DOLLARS 5 NON-DRAWDOWN) WHICH MARSHALL HAS PUT ON THE TABLE. THE QUESTION ARE HOW MUCH OF THIS COULD BE CASH OR NEAR CASH TO WHICH BA COULD EXPECT THE OTHER DEFENDANTS TO CONTRIBUTE AND HOW TO AVOID KNOCK-ON EFFECT ON THE OTHER CREDITORS. BA HAS MADE AN INITIAL APPROACH TO MCDONNELL DOUGLAS WHOSE CONCERN WAS NOT HOW MUCH EXIMBANK GOT BUT THAT THEY (MCDONNELL DOUGLAS) SHOULD GET NO LESS THAN THEIR COMPETITORS AIRBUS.

11. NEITHER WE NOR PARK SEE ANY BASIS FOR FURTHER INTERVENTION BY US WITH THE ADMINISTRATION BEFORE THE NEXT ROUND ON FRIDAY.

12. FCO PLEASE PASS ADVANCE COPIES TO: PS/SECRETARY OF STATE, PS/NO 10, PS/SECRETARY OF STATE FOR TRADE AND INDUSTRY, PS/ATTORNEY GENERAL, PS/FINANCIAL SECRETARY, PS/SECRETARY OF STATE FOR TRANSPORT, PS/MR RENTON (FCO), KNIGHTON, HOLMES, FORTNAM (DTP), BRAITHWAITE, O'NEILL, GRAY (FCO), AUST (LEGAL ADVISERS, FCO), AYLING (SOLS, DTI), GARDINER (LAW OFFICERS' DEPT), HEALEY, RICKFORD (DTI), GREGSON (CABINET OFFICE), WILSON (TREASURY).

WRIGHT

(ADVANCED AS REQUESTED)

LIMITED
HEAD/MAED MR BRAITHWAITE
HEAD/NAD MR O'NEILL
PS
PS/MR RENTON
PS/PUS

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DESKBY 070830Z
FM WASHINGTON 070715Z MARCH, 1985
TO IMMEDIATE F C O
TELEGRAM NUMBER 798 OF 7 MARCH.

YOUR TELNO 408: LAKER

SUMMARY

1. BA HAD TWO FURTHER MEETINGS WITH DRAPER AND ALBRIGHT TODAY. AT THE FIRST DRAPER CAME DOWN TO DOLLARS 28 MILLION (SPLITTING THE DIFFERENCE BETWEEN DOLLARS 33 MILLION AND WHAT HE SAID WAS BA'S POSITION, NAMELY DOLLARS 23 MILLION) OR BINDING MEDIATION ON THE BASIS OF SEALED BIDS FROM EACH PARTY TO A MEDIATOR. AT THE SECOND MEETING DRAPER SHOWED INTEREST IN A BA OFFER OF DOLLARS 25.5M INCLUDING DOLLARS 5M NON-DRAWDOWN. RESUMPTION OF DISCUSSION ON 8 MARCH.

DETAIL

2. BA MET DRAPER AFTER LUNCH. DRAPER REVEALED THAT HE HAD TALKED TO REGAN BUT DID NOT SAY WHEN. HE HAD ALSO TALKED TO WALLIS. NEITHER HAD GIVEN HIM ANY INDICATION THAT IN THE ADMINISTRATION'S VIEW THE MAXIMUM AMOUNT EXIMBANK COULD EXPECT TO OBTAIN WAS DOLLARS 20-22 MILLION. MOREOVER THE STATE DEPARTMENT HAD TOLD HIM THAT ACCORDING TO THE BRITISH EMBASSY (SIC), BA'S OFFER WAS DOLLARS 23 MILLION. HE THEREFORE PROPOSED TO SPLIT THE DIFFERENCE BETWEEN DOLLARS 33 MILLION (PARA 6 OF MY TELNO 783) AND DOLLARS 23 MILLION, PRODUCING DOLLARS 28 MILLION. ALTERNATIVELY WALLIS HAD SUGGESTED TO HIM THAT THE TWO PARTIES SHOULD AGREE ON A MEDIATOR. EACH PARTY WOULD GIVE THE MEDIATOR SEALED BIDS AND THE MEDIATOR, IN A BINDING DECISION, WOULD CHOOSE WHICHEVER BID WAS FURTHEST FROM EITHER PARTY'S POINT OF DEPARTURE (WHICH HE SPECIFIED AS DOLLARS 33 MILLION AND DOLLARS 23 MILLION). HE TURNED A DEAF EAR TO BA'S INSISTENCE THAT DOLLARS 23M WAS NOT THEIR POSITION AND THAT EXIMBANK COULD NOT LEGITIMATELY CLAIM INTEREST ARISING AFTER THE LIQUIDATION, SO THAT THE MAXIMUM POSSIBLE CLAIM WAS DOLLARS 21-22 MILLION. DRAPER INSISTED THAT THE ADMINISTRATION HAD CONVEYED NO SUCH MESSAGE TO HIM. BA AND EXIMBANK AGREED TO MEET AGAIN AT SIX IN THE EVENING.

3. MINISTER COMMERCIAL TELEPHONED THE STATE DEPARTMENT, GETTING MORRIS, TO CLEAR UP POSSIBLE STATE DEPARTMENT MISUNDERSTANDINGS AND HAVE THAT CLARIFICATION CONVEYED TO DRAPER. MORRIS SAID THAT HE WAS UNDER NO MISAPPREHENSION THAT BA WERE OFFERING DOLLARS 23 MILLION: HE HAD UNDERSTOOD PERFECTLY FROM YESTERDAYS CONVERSATION (PARA 9 OF MY TELNO 783) THAT BA'S OFFER WAS DOLLARS 18.2 MILLION: HE/WALLIS HAD CONVEYED THIS TO EXIMBANK. ALTHOUGH HE HAD UNDERSTOOD THAT BA WERE PREPARED TO TALK ABOUT BRIDGING THE GAP BETWEEN DOLLARS 18.2 MILLION AND DOLLARS 30 MILLION, HE HAD DELIBERATELY NOT CONVEYED THIS TO EXIMBANK, HE COMMENTED THAT DOLLARS 23 MILLION WAS IN ANY CASE A FIGURE WITHOUT ANY PARTICULAR MEANING IN THE CONTEXT OF BRIDGING A GAP BETWEEN DOLLARS 18.2 AND DOLLARS 30 MILLION. HE WAS UNABLE TO SUGGEST HOW DRAPER HAD GOT HOLD OF IT. MORRIS

HE WAS UNABLE TO SUGGEST HOW DRAPER HAD GOT HOLD OF IT. MORRIS FURTHER SAID THAT, WHILE IT WAS TRUE THAT THE ADMINISTRATION HAD NEVER SUGGESTED ANY PARTICULAR FIGURE TO DRAPER AT WHICH HE SHOULD SETTLE, IT HAD BEEN MADE ABUNDANTLY AND STRONGLY CLEAR TO HIM BOTH THAT THE PRESIDENT WANTED A SETTLEMENT AND THAT IN US AS WELL AS JERSEY LAW, EXIMBANK WAS NOT ENTITLED TO POST LIQUIDATION INTEREST.

4. MORRIS ALSO SAID, ON THE MEDIATION POINT, THAT WALLIS HAD CONVEYED TO DRAPER THE TECHNIQUE SHULTZ HAD USED IN HIS DAYS AS A LABOUR MEDIATOR. THIS WAS INDEED A SEALED BID APPROACH WITH THE MEDIATOR'S DECISION BINDING, BUT THE GROUND RULES WERE AGREED BETWEEN THE TWO SIDES FIRST AND IT WAS NOT NECESSARY THAT THE MEDIATOR SHOULD ACCEPT THE BID OF THE PARTY WHICH HAD MOVED FURTHEST NUMERICALLY FROM ITS STARTING POSITION.

5. MINISTER COMMERCIAL ALSO SPOKE TO DAWSON, REGAN'S EXECUTIVE ASSISTANT IN THE WHITE HOUSE (WHO, WE HEARD FROM OTHER SOURCES, SPOKE TO ALBRIGHT THIS MORNING TO GIVE HIM AN ACCOUNT OF MY PHONE CALL TO REGAN). HE SAID THAT FOLLOWING MY TELEPHONE CONVERSATION WITH REGAN LAST NIGHT, THE TALKS NOW LOOKED AS IF THEY MIGHT BE HEADING FOR BREAKDOWN. DRAPER WAS SHOWING HIMSELF UNABLE OR UNWILLING TO RECOGNISE THAT BA COULD NOT POSSIBLY PAY EXIMBANK 100 PER CENT AND MORE OF THEIR MAXIMUM POSSIBLE ENTITLEMENT. AGREEMENT WITH EXIMBANK ON SUCH TERMS WOULD HAVE A MASSIVE ESCALATOR EFFECT AND DESTROY THE SETTLEMENT WITH THE OTHER PARTIES INVOLVED. DRAPER MIGHT OF COURSE MERELY BE NEGOTIATING TOUGHLY, BUT IF HE MEANT WHAT HE WAS SAYING (AND CROWE EXPLAINED WHAT THAT WAS) SUCCESS WAS IMPOSSIBLE. DAWSON SAID HE WOULD ''TAKE IT UP''
.

6. WHEN BA MET DRAPER AGAIN AT 6.00PM, DRAPER - AWKWARDLY BUT DELIBERATELY - SET ABOUT DISAVOWING THAT THE BRITISH EMBASSY HAD BEEN THE SOURCE OF THE ALLEGED DOLLARS 23M BA OFFER AND ALLUDED VAGUELY TO AMBASSADOR PRICE AS THE SOURCE. ON THE SUBSTANCE BA SAID THAT THEY WERE PREPARED TO GO UP TO DOLLARS 21M - 22M SUBJECT TO CLEARING WITH HMG AND OTHER CREDITORS AND DEFENDANTS. DRAPER INDICATED ACCEPTANCE OF DOLLARS 21M-22M PROVIDING THIS EXCLUDED NON-DRAWDOWN, ON THE BASIS THAT IT WAS VALUELESS. THIS HAD TO INCLUDE DOLLARS 8M OR WHATEVER LAKER RECEIVED IN CASH, THE BALANCE TO BE MADE UP IN INTEREST ADJUSTMENT. BA IMPLICITLY REJECTED THIS. MARSHALL MADE THE POINT THAT BA WERE CONSIDERING BUYING FURTHER 757S AGAINST THE DRAWDOWN, BUT THAT EXIMBANKS ATTITUDE MADE SUCH A PURCHASE DIFFICULT. HE OFFERED INSTEAD DOLLARS 25.5 INCLUDING DOLLARS 10M NON-DRAWDOWN. EXIMBANK REJECTED THIS. MARSHALL THEN SUGGESTED DOLLARS 25.5M, INCLUDING DOLLARS 5M NON-DRAWDOWN. EXIMBANK WERE INTERESTED ON THE BASIS THAT THIS INCLUDED DOLLARS 8M, OR WHATEVER LAKER RECEIVED, CASH. BA MADE CLEAR THEIR BASIS, NAMELY CLEARANCE WITH HMG AND WITH OTHER CREDITORS FOR KNOCK-ON EFFECT. IT WAS AGREED TO DISCUSS FURTHER ON 8 MARCH AFTER FURTHER REFLECTION BY BA.

7. DRAPER IN THE COURSE OF THE DISCUSSION POINTEDLY ASSERTED THAT
A. NOBODY TOLD HIM WHAT TO DO ON FIGURES
B. AMBASSADOR PRICE IN PARTICULAR HAD NO AUTHORITY OVER HIM.

8. LIKEWISE - FOR WHAT IT IS WORTH - DURING THE DISCUSSION EXIMBANK VALUED HALF OF THE NON-DRAWDOWN AS DOLLARS 6OM RATHER

8. LIKEWISE - FOR WHAT IT IS WORTH - DURING THE DISCUSSION EXIMBANK VALUED HALF OF THE NON-DRAWDOWN AS DOLLARS 60M RATHER THAN DOLLARS 45M.

9. AFTER THE MEETING DRAPER PHONED MARSHALL BY PRE-ARRANGEMENT. HE SAID THAT EXIMBANK'S CALCULATION OF THE PRESENT VALUE OF THE INCREASED INTEREST ON BA LOANS WAS BASED ON EXIMBANK'S CURRENT COST OF LENDING AT 11.5 PERCENT. BA'S CALCULATION HAD BEEN BASED ON THEIR CURRENT LOAN RATE OF 9.25 PERCENT. EXIMBANK'S CALCULATION WOULD REQUIRE A CORRESPONDINGLY LARGER INCREASE IN INTEREST RATES TO ACHIEVE THE SAME PRESENT VALUE. MARSHALL SAID HE WAS RETURNING TO LONDON TONIGHT (WEDNESDAY) AND WOULD RETURN ON 8 MARCH. DRAPER SUGGESTED THAT HE AND MARSHALL COULD SETTLE THE MATTER BY TRANSATLANTIC TELEPHONE CONVERSATION. (PARK REGARDED THIS AS UNREALISTIC AND EXPECTS MARSHALL TO RETURN).

10. WE UNDERSTAND BA ARE CALCULATING HOW THEY COULD MAKE UP THE DOLLARS 20.5M (DOLLARS 25.5 LESS DOLLARS 5 NON-DRAWDOWN) WHICH MARSHALL HAS PUT ON THE TABLE. THE QUESTION ARE HOW MUCH OF THIS COULD BE CASH OR NEAR CASH TO WHICH BA COULD EXPECT THE OTHER DEFENDANTS TO CONTRIBUTE AND HOW TO AVOID KNOCK-ON EFFECT ON THE OTHER CREDITORS. BA HAS MADE AN INITIAL APPROACH TO MCDONNELL DOUGLAS WHOSE CONCERN WAS NOT HOW MUCH EXIMBANK GOT BUT THAT THEY (MCDONNELL DOUGLAS) SHOULD GET NO LESS THAN THEIR COMPETITORS AIRBUS.

11. NEITHER ME NOR PARK SEE ANY BASIS FOR FUPTHER INTERVENTION BY US WITH THE ADMINISTRATION BEFORE THE NEXT ROUND ON FRIDAY.

12. FCO PLEASE PASS ADVANCE COPIES TO: PS/SECRETARY OF STATE, PS/NO 10, PS/SECRETARY OF STATE FOR TRADE AND INDUSTRY, PS/ATTORNEY GENERAL, PS/FINANCIAL SECRETARY, PS/SECRETARY OF STATE FOR TRANSPORT, PS/MR RENTON (FCO), KNIGHTON, HOLMES, FORTNAM (DTP), BRAITHWAITE, O'NEILL, GRAY (FCO), AUST (LEGAL ADVISERS, FCO), AYLING (SOLS, DTI), GARDINER (LAW OFFICERS' DEPT), HEALEY, RICKFORD (DTI), GREGSON (CABINET OFFICE), WILSON (TREASURY).

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TO FLASH WASHINGTON
TELEGRAM NUMBER 408 OF 6 MARCH

YOUR TELNO 783: LAKER

1. MINISTERS HAVE CONSIDERED THE POSITION SET OUT IN YOUR TUR. THEY AGREE WITH YOUR RECOMMENDATION.
2. MINISTERS WANT TO SEE THE EXIM POSITION SETTLED BUT ARE CONCERNED THAT THE POTENTIAL ESCALATION OF ANY MONIES ABOVE DOLLARS QUARTER MILLION PAID TO EXIM ON THE CLAIMS OF OTHER SECURED CREDITORS IS UNQUANTIFIABLE IN ADVANCE. IT IS NO MORE THAN PARK'S JUDGEMENT THAT MONIES PAID IN ONE WAY RATHER THAN ANOTHER MAY NOTATTRACT THIS ESCALATION. THE MORE THAT IS PAID TO EXIM IN WHICHEVER FORM, THE GREATER THE POTENTIAL FOR ESCALATION. YOU ARE NO DOUBT USING THIS POINT IN ADDITION TO THAT IN YOUR PARA 9, WITH WHICH WE AGREE. OUR AIM IS THAT BA SHOULD SLUG IT OUT TO AN ACCEPTABLE CONCLUSION OVER THE NEXT 24 HOURS OR SO.
3. OUR UNDERSTANDING FROM YOUR TUR AND TELECON MARSHALL/KNIGHTON LAST NIGHT IS THAT BA'S LAST FIRM OFFER IS DOLLARS 18.2 MILLION INCLUDING NON-DRAW DOWN, BUT THAT BA HAD TENTATIVELY SPOKEN AT THE END OF THE FIRST SESSION OF UP TO A FURTHER DOLLARS 5 MILLION, IN THE FORM OF ADJUSTMENT OF INTEREST RATES RATHER THAN IMMEDIATE CASH. OUR UNDERSTANDING IS THAT THE MENTION OF THIS (LIKE THE EARLIER OFFER) WAS CONDITIONAL ON A SATISFACTORY POSITION THEREAFTER BEING REACHED ON THE OVERALL PACK-AGE, INCLUDING THE MONIES RECEIVED BY THE OTHER CREDITORS AND THE CONTRIBUTIONS OF OTHER CONTRIBUTORS FOLLOWING AN INCREASE IN THE PAYMENT TO EXIM: AND ALSO AD REFERENDUM TO HMG. WE THINK THEREFORE THAT BA SHOULD PRESS HARD TO SETTLE AT DOLLARS 18.2

MILLION (WITH THE POLITICAL SUPPORT OF YOUR INTERVENTION LAST NIGHT AND MR RIDLEY'S HERE TODAY) AND USING THE ARGUMENT THAT AT THIS FIGURE EXIM ARE GETTING 80-90 PERCENT OF THEIR CLAIM AND THAT SUCH LARGE SUMS MAY YET WRECK THE SETTLEMENT. IF THEY HAVE TO REVERT TO THEIR TENTATIVE PROPOSAL OF UP TO DOLLARS 23 MILLION THEY SHOULD NOT REMOVE THE CONDITIONALITY ON IT. THEY SHOULD KEEP IN TOUCH WITH DTP.

4. MR RIDLEY HAS SEEN AMBASSADOR PRICE TO SPEAK ON LINES SIMILAR TO YOUR PARA 9 AND TO SEEK PRICE'S ASSISTANCE IN DELIVERING A MORE REASONABLE NEGOTIATING POSITION FROM EXIM. PRICE PROMISED TO TRY TO HELP BEFORE BA SEE DRAPER LATER TODAY. HE IMPLIED THAT DRAPER IS OUT ON HIS OWN. HE APPEARED TO TAKE ON BOARD THAT DOLLARS 18 MILLION WAS GENEROUS COMPARED WITH EXIM'S BASIC CLAIM OF DOLLARS 21 MILLION, FAR MORE THAN OTHER CREDITORS WERE LIKELY TO GET, BUT MIGHT CAUSE ESCALATION. HE ALSO APPEARS SEIZED OF THE URGENCY. HE RECOGNISED (PLEASE PROTECT) THAT A PAYMENT TO LAKER WAS NECESSARY.

HOWE

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MR GARDINER, LAW OFFICERS
MR GREGSON, CABINET OFFICE
MR WILSON, HMTREASURY
MR AUST - HA

NOTE OF THE SECRETARY OF STATE'S MEETING WITH THE US AMBASSADOR ON 6 MARCH 1985
HELD IN ROOM 21, HOUSE OF COMMONS

Present:

The Secretary of State
Mr Knighton
Mr Ayling
Mr Allen

Ambassador Price

Mr Price had been called in by the Secretary of State following the discussion at MISC 112 earlier that morning.

The Secretary of State recalled that the Prime Minister had spoken to the President on her recent visit to Washington and that they had agreed on the importance of sorting out a settlement of the Laker anti-trust case. But ExIm were proving to be a stumbling block. Whereas other major creditors were prepared to settle for $¼m they had claimed $65m, which went well beyond any rights we believe they might have even if the case went to court. Our legal advice was that under Jersey law their claim could be worth nothing and that even applying US law their maximum claim in an involuntary liquidation would be some $20m. In the informal discussions with British Airways the previous day, when BA had made a tentative offer of $18m, ExIm had still stuck out for $33m. The ExIm claims were not only large in themselves: there was a very real danger that they would cause the tentative agreement with the other creditors to become unravelled. The Secretary of State knew that the President was doing his best. But the Prime Minister had asked him to say that if the matter was not settled the political damage on both sides of the Atlantic could be very serious. ExIm was now the stumbling block.

Mr Price noted that ExIm had already moved from their initial claim of $65m to $33m. He understood that the previous day's discussions had been positive, and he felt that the gap should now be bridgeable. The importance of settling the matter was well understood in Washington. Mr Price had

himself spoken to the President and Messrs Shultz, Regan, Brock and Wallis. He had also spoken to Mr Allbright at ExIm, though not to Draper. He added, in confidence, that he believed Draper, who was a stubborn negotiater, was concerned with the presentation of any settlement, and especially about comparisons between what ExIm, and what Mr Beckman and Sir Freddie Laker, derive. But Mr Price's view was that that had to be viewed against the background of the undesirable consequences of not reaching a settlement. Mr Price was sure that the political and diplomatic consequences of not reaching a settlement had been explained to Mr Draper as well as they could, though, quite naturally, he had not been told to reach agreement at a particular figure.

In further discussion, Mr Price indicated that the ExIm lawyers advising Mr Draper did not appear to accept the advice of the State Department lawyers about the position under Jersey law of interest on the outstanding claim. Mr Ayling commented that his impression was that the State Department legal advisors accepted that ExIm's claim should exclude post liquidation interest and be limited to $22m. They also understood that the Royal Bank of Canada, Eurocontrol, and UK Air Travel Reserve Fund were not receiving payment of anything like the proportion of their claims was now being offered to ExIm.

In conclusion, the Secretary of State re-emphasised that ExIm's excessive claims were proving a stumbling block to a settlement, and risked jeopardising the position reached with the other creditors. It would be difficult to hold them even at the level of British Airways' present offer of $18 million. There was a significant body of opinion within the British Government which would like to fight the matter out if it could not be settled on reasonable terms. He believed that there were extreme risks for both sides if the matter was not cleared up quickly. He understood that British Airways

would be negotiating further with ExIm that day. Mr Price agreed that the matter ought to be settled, and said he had advised the importance of this to Washington as candidly as he could. He asked when the next round of discussions was due to start, and left the impression that he would be in touch with Washington again.

R. A. Allan

R A ALLAN
PS/Secretary of State
S12/04
212 3751

7 March 1985

cc: PS/Mr Spicer
PS/Sir Peter Lazarus
Mr Knighton
Mr Stevens
Mr Blanks
Mr Ayling (DTI)
Mr Fortnam
Mr Rhodes
PS/Members of MISC 112
PS/Sir Robert Armstrong

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TO IMMEDIATE F C O
TELEGRAM NUMBER 783 DATED 5 MARCH

LAKER

SUMMARY

1. BA HAD TWO MEETINGS WITH DRAPER AND ALBRIGHT (EXIMBANK) TODAY. AT THE FIRST BA OFFERED A TOTAL OF DOLLARS 18.2 MILLION INCLUDING NON-DRAWDOWN: EXIMBANK HELD OUT FOR DOLLARS 30 MILLION PLUS DOLLARS 10 MILLION NON-DRAWDOWN. AT THE END OF THE MEETING BA URGED EXIMBANK TO INCLUDE NON-DRAWDOWN WITHIN THEIR DOLLARS 30 MILLION DEMAND. THE RESULTING GAP WOULD BE DOLLARS 10 OR DOLLARS 12 MILLION WHICH MIGHT BE BRIDGEABLE IN SOME WAY. THIS PROMPTED EXIMBANK TO SUGGEST THE SECOND MEETING LATER IN THE DAY. AT THE SECOND MEETING EXIMBANK CAME NO LOWER THAN DOLLARS 33 M, BUT WERE KEEN TO HAVE FURTHER DISCUSSIONS. CLEAR SIGNALS FROM VARIOUS SOURCES THAT DRAPER, FOR ALL HIS TOUGH NEGOTIATING, UNDER STRONG PRESSURE FROM WHITE HOUSE AND THAT DISCUSSION SHOULD INDEED CONTINUE.

DETAIL

1. MARSHALL (BA) AND PARK (LINKLATER AND PAINE) SAW DRAPER AND ALBRIGHT (EXIMBANK) OVER LUNCH TODAY. THE ATMOSPHERE OF THE MEETING WAS MUCH BETTER THAN PREVIOUSLY, WITH GREATER WILLINGNESS ON EXIMBANK'S PART TO LISTEN. WHEN THEY GOT DOWN TO BUSINESS, BA SAID THEY WERE WILLING TO INCREASE THEIR OFFER BY DOUBLING THEIR COMMITMENT FEE ON THEIR BOEING 757 LOAN, PRODUCING DOLLARS 3.2 MILLION, AND BY INCREASING THE INTEREST RATE ON THE LOAN BY 1.4 PERCENT PER ANNUM, PRODUCING DOLLARS 5 MILLION (PRESENT VALUE). TOGETHER WITH NON-DRAWDOWN THIS TOTALLED DOLLARS 18.2 MILLION. IN REPLY DRAPER INSISTED THAT HE WANTED A MINIMUM OF DOLLARS 30 MILLION PLUS THE VALUE OF THE NON-DRAWDOWN, TOTALLING DOLLARS 40 MILLION. HE PROPOSED THAT THIS SHOULD BE ACHIEVED IN PART BY INCREASING THE INTEREST RATE ON ALL OUTSTANDING LOANS ON 737S AND 757S TO 13 PERCENT. THIS WOULD, THEY CLAIMED, PRODUCE DOLLARS 24 MILLION (ON MARSHALL'S CALCULATION DOLLARS 28M IS NEARER THE MARK).

2. THERE WAS EXTENSIVE DISCUSSION ON THE NON-DRAWDOWN. DRAPER ARGUED THAT IT WOULD NOT HAVE BEEN USED ANYWAY. BA ARGUED THAT, WHILE IT WOULD NOT SHOW ON THE BALANCE SHEET IMMEDIATELY, IT WAS STILL A BENEFIT WHICH COULD BE DISCLOSED PUBLICLY. EXIMBANK WERE UNCONVINCED.

3. IN DISCUSSION ON THE LEGAL VALIDITY OF THE POST-LIQUIDATION INTEREST CLAIM, DRAPER SAID DISMISSIVELY THAT HE DID NOT LISTEN TO THE STATE DEPARTMENT LAWYERS - THAT WAS ANOTHER WORLD.

4. IN DISCUSSION OF SIR FREDDIE LAKER, DRAPER FOR THE FIRST TIME GAVE A HINT OF ACCEPTING THE NEED FOR PAYMENT TO HIM BY REVEALING CONCERN OVER THE POSSIBILITY THAT LAKER MIGHT NOT GIVE A RELEASE WHICH INCLUDED EXIMBANK.

5. THE DISCUSSION WAS SUSPENDED BECAUSE DRAPER HAD TO GO TO ANOTHER MEETING. BA ASKED EXIMBANK TO INCLUDE NON-DRAWDOWN AS PART OF DRAPER'S FIGURE OF DOLLARS 30 MILLION, LEAVING A GAP TO BE BRIDGED IN THE FURTHER DISCUSSION OF DOLLARS 30 MILLION AGAINST DOLLARS 18 MILLION. IT MIGHT BE POSSIBLE TO ACHIEVE THIS. THIS PROMPTED DRAPER TO SUGGEST ANOTHER MEETING AT 5 PM. BA'S OVERALL IMPRESSION OF THE MEETING WAS THAT DRAPER WAS NOW TRYING TO FIND A SOLUTION BUT STILL HOLDING OUT FOR AN EXCESSIVE AMOUNT.

6. THE MEETING AT 5PM WAS SHORT. DRAPER DEMANDED DOLLARS 33M MADE UP AS FOLLOWS:
A. DOLLARS 3M COMMITMENT FEE
B. DOLLARS 5M FRONT END FEE, APPARENTLY A RECENT EXIMBANK INNOVATION UNDER WHICH BORROWERS PAY UP FRONT 2 PERCENT OF LOANS APPLIED FOR. FOR BA DRAPER CALCULATED DOLLARS 250M.
C. DOLLARS 10M NON DRAWN DOWN
D. DOLLARS 15M (PRESENT VALUE) ADJUSTMENT OF INTEREST RATES.

7. DRAPER SAID HE WANTED A CASH SUM NO LESS THAN THAT PAID TO LAKER.

8. BA SAID THAT THEIR ''SHAREHOLDER'' WAS ALREADY DISPLEASED THAT, BY SUGGESTING DOLLARS 13 M (PLUS DOLLARS 10M NON-DRAWDOWN), THEY HAD EXCEEDED THEIR AUTHORITY. DRAPER SAID THAT HE HAD THOUGHT HE WAS NEGOTIATING WITH PRINCIPALS AND THAT HE WAS NEGOTIATING FREELY AND IN GOOD FAITH. BA ARGUED THAT AT DOLLARS 23M, WITHOUT TAKING ACCOUNT OF THE NONDRAWDOWN, EXIMBANK WOULD BE GETTING MORE THAN THEIR DUE. DRAPER ARGUED THAT IT WOULD NOT BE BY MUCH, WOULD NOT AFFECT OTHER CREDITORS AND BY THE DEVICES HE WAS SUGGESTING

WOULD NOT INVOLVE THE OTHER DEFENDANTS. BA ARGUED THAT EXIMBANK SHOULD NOT GET MORE THAN 100 PERCENT. DRAPER WAS KEEN TO CONTINUE THE DISCUSSION AFTER BA HAD TALKED TO THEIR PRINCIPALS, PREFERABLY THIS EVENING OR FIRST THING IN THE MORNING: HE WAS EVEN WILLING TO GO OUT TO DULLES AIRPORT TO MEET MARSHALL THERE BEFORE THE LATTERS PLANNED DEPARTURE AT MIDDAY ON 6 MARCH. IT WAS LEFT THAT BA WOULD CONTACT DRAPER, BY IMPLICATION ON 6 MARCH.

9. MINISTER COMMERCIAL SPOKE TO MORRIS (STATE DEPARTMENT) TO EXPRESS DISAPPOINTMENT AT THE CONTINUED STAND-OFF AND LACK OF REASONABLENESS ON EXIMBANK'S PART, SUGGESTING THAT THE SETTLEMENT WE WERE ALL AFTER WAS SLIPPING AWAY. HE EMPHASISED THE POINT ABOUT EXIMBANK NOT BEING ENTITLED, UNDER JERSEY OR US LAW, TO MORE THAN ABOUT DOLLARS 20M. MORRIS SAID THAT THE STATE DEPARTMENT HAD TOLD DRAPER THIS. IF HE WAS NOT RESPONDING, IT WAS BECAUSE HE WAS NOT TAKING ANY NOTICE OF THE STATE DEPARTMENT. SHULTZ HAD SAID DRAPER SHOULD SPEAK TO DON REGAN. HE COULD ONLY SUGGEST THAT H SHOULD DO SO.

10. SIMULTANEOUSLY MARSHALL SPOKE TO THE PRESIDENT OF MCDONNELL DOUGLAS IN CALIFORNIA (MCDONELL DOUGLAS HAD BEEN PUTTING ON PRESSURE OF HER OWN THROUGH REGAN'S STAFF). HE SAID THAT THE WHITE HOUSE HAD EXERCISED VERY STRONG PRESSURE ON DRAPER AND GIVEN HIM 48 HOURS, AND PREFERABLY 24, TO SETTLE. (PRESUMABLY FROM THE START OF TODAYS DISCUSSIONS). THE WHITE HOUSE WANTED NO INTERNATIONAL INCIDENT OR PROBLEMS WITH THE UK. ACCORDING TO MCDONNELL DOUGLAS, THE STATE AND COMMERCE DEPARTMENTS HAD ALSO PUT PRESSURE ON MCDONNELL DOUGLAS.

11. H CALLED REGAN THIS EVENING. HE ASKED ABOUT THE NEED FOR LAKER TO RECEIVE MONEY AND SAID THAT DRAPER WAS ''NEGOTIATING'' AND HAD TO HAVE A GOOD STORY TO TELL TO CONGRESS. HIS EXECUTIVE ASSISTANT HAD SPOKEN TO DRAPER TWICE (UNCLEAR WHEN). THEY HAD NOT SIGNED OFF. HE (REGAN) WOULD TAKE A CLOSE LOOK IN THE MORNING.

12. MY RECOMMENDATION IS THAT DRAPER SHOULD BE ALLOWED TO SWEAT THROUGH MOST OF TOMORROW, THAT BA SHOULD CONTACT LATER IN THE DAY AND THAT THEY SHOULD BE IN A POSITION TO SAY THAT THEY HAD SPOKEN TO THEIR PRINCIPALS: THAT THEIR PRINCIPALS WERE UNHAPPY THAT BA HAD GONE AS FAR AS THEY HAD: THAT THERE WAS NO QUESTION OF GOING ANY FURTHER: AND THAT BA HOPED A CONCLUSION COULD NOW BE REACHED. WE HAVE SPOKEN TO PARK, WHO AGREES.

13. FCO PLEASE ADVANCE COPIES TO: PS/SECRETARY OF STATE, PS/NO 10, PS/SECRETARY OF STATE FOR TRADE AND INDUSTRY, PS/ATTORNEY GENERAL, PS/FINANCIAL SECRETARY, PS/SECRETARY OF STATE FOR TRANSPORT, PS/MR RENTON (FCO), KNIGHTON, HOLMES, FORTNAM (DTP), BRAITHWAITE, O'NEILL, GRAY (FCO), AUST (LEGAL ADVISERS, FCO), AYLING (SOLS, DTI), GARDINER (LAW OFFICERS' DEPT), HEALEY, RICKFORD (DTI), GREGSON (CABINET OFFICE), WILSON (TREASURY).

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01-405 7641 Ext. 3040/3229
Communications on this subject should be addressed to
THE LEGAL SECRETARY
ATTORNEY GENERAL'S CHAMBERS

ATTORNEY GENERAL'S CHAMBERS,
LAW OFFICERS' DEPARTMENT,
ROYAL COURTS OF JUSTICE,
LONDON, W.C.2.

R A Allan Esq.
Private Secretary
Secretary of State for Transport
2 Marsham Street
London SW1

5 March 1985

Dear Allan,

LAKER: ATTEMPTED SETTLEMENT.

in meeting folder.

1. I refer to your letter of 4 March to Turnbull.

2. As I reported by telephone last night, the Attorney General has seen the proposals for a new offer by British Airways to Eximbank in an effort to reach a settlement. The Attorney General has noted that in law there is no problem about such a settlement but it must be a policy decision. He regrets that Eximbank appears to have dismissed outright the advice of the Jersey Law Officers.

3. I am sending copies of this letter to the Private Secretaries to the Prime Minister, the Foreign Secretary, Chancellor of the Exchequer and Financial Secretary, Secretary of State for Trade and Industry and Sir Robert Armstrong.

Yours ever,

Richard Gardiner

R K GARDINER

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AEROSPACE : CAA Review
Pt 3

iii. If not, what are the next steps?

Settlement terms

4. The proposed terms are set out in the Annex to PS/Mr Ridley's letter of 4 March. The cost has increased since January from $52.5 million to $69 million. The increase is chiefly due to $10 million extra for Eximbank and the likely "multiplier effect" on claims by other secured creditors.

5. Increased costs of this order will be unwelcome, but the Group is unlikely to accept them as preferable to the damage which would ensue if legal processes went ahead. The following points arise.

i. The Annex appears to allow an increase of $8 million in payments to secured creditors other than Eximbank as a result of the "multiplier effect". The Group will want to consider the assumptions on which this figure is based and to assess the margin for error.

ii. The costing assumes that the Inland Revenue will be ready and able to forgo an increase in their own claim on the liquidation. You will want confirmation from the Financial Secretary, Treasury that the Revenue's claim need not be an obstacle if a settlement seems otherwise to be a possibility.

iii. The increased cost of the new settlement terms falls entirely on BA whose contribution will increase from $20 million to $35-40 million. This would leave them paying between 51 and 58 per cent of total settlement costs, compared with 40 per cent or less envisaged in January. This will be taken in some quarters as an admission of some kind and will have political, as well as financial, implications.

Next steps

6. Formal liquidation proceedings are likely to resume at or, soon after, the end of this week if there is no agreement. They would be

CONCLUSIONS

10. You will wish to reach conclusions on:

i. if the talk with Eximbank has gone well, any further action to achieve a speedy settlement;

ii. if the talk has gone badly, whether:

a. to continue to pursue a settlement by diplomatic means and/or by a further improvement in the offer; or

b. to allow the legal proceedings to go ahead, and, if so, how to mitigate the damage.

P L GREGSON

5 March 1985

10 DOWNING STREET

From the Private Secretary

Prime Minister ①

A meeting of MISC 112 has been arranged for Wednesday. Meanwhile Mr Ridley seeks agreement for BA to raise its offer to EXIM in an effort to reach a settlement. This could cost an extra $20 million, all of which would fall to BA.

Despite this, the Foreign Secretary, Financial Secretary and Attorney General all agree that this should be done, before the discovery process start up again.

Agree?

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DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

Andrew Turnbull Esq.,
PS/Prime Minister
10 Downing Street,
London, S.W.1

4 March 1985

Dear Andrew,

LAKER: ATTEMPTED SETTLEMENT

We have now discussed with the British Airways' negotiators the situation following their last round of discussions with Exim and the position which they should take in their resumed discussions in Washington at lunch time tomorrow. We must give them the Government's view on what further offers we should find acceptable before tomorrow's meeting.

2 We summarised the Exim claim in Dinah Nichols' letter of 1 March. Further contacts over the weekend suggest that lawyers in the Administration, as well as Exim, have a rooted objection to accepting the the argument based on Jersey law that they do not have a valid claim to principal outstanding from their loan. On the other hand there may be greater acceptance of the proposition that interest after the date of liquidation would not count. Exim's claim for principal is some $21 million. Exim also continue to object to any payment to Sir Freddie Laker (and British Airways, for their part, consider that Laker's undertaking not to pursue further litigation ~~liquidation~~ is an essential part of a settlement). Exim also argue strenuously that, among the major creditors, they are being asked to give up more than anybody else by the formula originally proposed of $¼ million payment to each such creditor.

3 In these circumstances British Airways consider that in order to be in a serious negotiation with Exim they need to be in a position to offer some $10 million in cash (now or later) and some $10 million by the foregoing of drawing rights on Exim referred to in my earlier letter. They would hope that other creditors would disregard the foregoing of drawing rights in considering whether to increase their own claims if Exim get more than $¼ million. And they contemplate that part of the $10 million in cash would be paid by an increase of interest rates on existing BA loans from Exim, which they would also hope other creditors would be prepared to see as not calling for an increase in their own settlement payments.

Dinah Nicholl's

4 The effect of these propositions on the potential cost of the settlement is shown in the Annex. When Ministers were considering the matter earlier, the overall cost was estimated at some

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8 Mr Ridley hopes that it will be possible for a meeting of MISC 112 to be held on Wednesday or Thursday so that colleagues concerned can consider the situation now emerging. But meanwhile he hopes that the Prime Minister and other colleagues will agree that British Airways should be empowered to make a further offer on the lines indicated above. We should like this agreement by 6.00 pm this evening so that the negotiators can be told before they leave for Washington, or failing that, by not later than 10 am London time tomorrow.

9 I am sending copies of this letter to the Private Secretaries to the Foreign Secretary, Chancellor of the Exchequer and the Financial Secretary, Secretary of State for Trade and Industry, the Attorney General and to Sir Robert Armstrong.

Yours,

Richard Allan.

R A ALLAN
Private Secretary

CONFIDENTIAL

CC NO

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

Prime Minister (2)
Difficulties!

Andrew Turnbull Esq.,
PS/Prime Minister
10 Downing Street,
London, S.W.1

AT 1 March 1985

Dear Andrew,

LAKER: ATTEMPTED SETTLEMENT

The Prime Minister will wish to know that the discussions between British Airways and Exim Bank yesterday in Washington went badly (see Washington telno 730 attached). Despite the response of the President when the Prime Minister raised the matter with him, and the fact that we know that a message was conveyed to Exim that the Administration would like to see the matter settled, Exim were not in a serious negotiating posture.

Exim claim $65 million. This is the aggregate of the principal and interest due at the date of winding up (after deducting the value of security) plus interest since winding up. But on the assumption that this is an insolvent winding up, Jersey law would not allow post winding-up interest and would require the security to be valued in sterling at the date of the realisations. On this view, Exim would have no claim. There is an alternative view of Jersey law but even this would only entitle Exim to claim $11.5 million. It was on this basis that British Airways had offered only a quarter of a million pounds to Exim formally as part of the settlement (the same as the other major financing creditors have in principle agreed to accept), while also offering to forego a right to draw on Exim loans which, because of changes in interest rates, would have been worth on Exim's original assessment some $15 million to them.

Yesterday Exim opened again with their $65 million claim. After vigorous argument they made a counter-proposal that they should receive $50 million: $25 million in cash as part of the settlement and $25 million through some kind of adjustment of other transactions between themselves and British Airways (in which they would now count foregoing of drawing rights referred to above at only $10 million.)

This posture showed the two sides as so far apart that British Airways felt they had no option but to withdraw again from the discussion.

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TO IMMEDIATE FCO
TELEGRAM NUMBER 730 OF 1 MARCH

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ADVANCE COPY

IMMEDIATE

MY TELNO 720
LAKER SETTLEMENT

1. PARK (LINKLATERS) AND MARSHALL (BA) REPORTED ON THIS AFTERNOON'S MEETING WITH DRAPER (EXIMBANK). THE MEETING HAD GONE VERY BADLY WITH EXIMBANK REITERATING THEIR FAMILIAR ARGUMENTS AND CONTINUING TO INSIST ON POST LIQUIDATION INTEREST. PARK AND MARSHALL SAID THAT IT WAS AS IF NOTHING HAD HAPPENED OVER THE PAST 10 DAYS.

2. BA HAD BEGUN AS A GOODWILL GESTURE BY HANDING OVER A LETTER SAYING THAT THEY WOULD NOT DRAW DOWN DOLLARS 28M OF THE LOAN DUE TODAY, AND HAD STRESSED THAT SINCE THE MORNING ALL OF THE OTHER FINANCE CREDITORS WERE COMMITTED IN WRITING TO THE PROPOSED SETTLEMENT.DRAPER HAD SAID THAT EXIM WERE NOT INTERESTED IN THE OFFER OF DOLLARS 250,000 PLUS NO DRAW DOWN WHICH EXIM NOW ESTIMATED TO BE WORTH ONLY DOLLARS 10M RATHER THAN DOLLARS 14.7M WHICH WAS THEIR PREVIOUS ESTIMATE. BA URGED EXIM, HAVING REJECTED BA'S OFFER, TO MAKE A COUNTER OFFER AND DRAPER PROPOSED DOLLARS 25M IN CASH PLUS DOLLARS 25M IN OTHER FORMS OF PAYMENT OF WHICH THE UNDERTAKING NOT TO DRAW DOWN ON THE EXIMBANK LOAN WOULD COUNT AS DOLLARS 10M . BA HAD MADE IT CLEAR THAT THIS WAS NOT FEASIBLE.

3. IN THE COURSE OF DISCUSSION EXIM SAID THAT THEY DID NOT BELIEVE THAT THE JUDGEMENT OF US COURTS WOULD BE ENFORCIBLE IN THE UK AND TOOK THE LINE THAT HMG WOULD SIMPLY HAVE TO FIND THE SUMS OF MONEY CONSISTENT WITH THE SETTLEMENT TERMS EXIM WERE SEEKING. THEY WERE ALSO VERY SCEPTICAL ABOUT BA'S EXPLANATIONS OF THE JERSEY LAW POSITION AND AGAIN MADE CONSTANT REFERENCE TO SIR FREDDIE LAKER WHO DRAPER REVEALED HAD CONTACTED HIM OR ALLBRIGHT TO ASK ABOUT EXIM'S OBJECTIONS TO HIS RECEIVING PAYMENT. EXIM TOLD BA THAT THEY HAD EXPECTED A NEW PROPOSAL FROM THEM. BA HAD SAID THAT IN VIEW OF THE DISCUSSIONS WHICH HAD TAKEN PLACE OVER THE PAST 10 DAYS THEY HAD UNDERSTOOD THAT ANEGOTIATION ON THEIR EXISTING PROPOSALS WOULD BE POSSIBLE. THE MEETING ENDED WITHOUT ANY AGREEMENT ON A FURTHER MEETING.

4. THE NEGOTIATIONS HAVE CLEARLY RUN INTO THE DIFFICULTY THAT THE AGREEMENT REACHED DURING THE PRIME MINISTER'S VISIT CANNOT EASILY BE QUANTIFIED. EXIM HAVE MADE A SMALL MOVEMENT IN THEIR POSITION BUT THIS CLEARLY REMAINS WAY BEYOND THE BOUNDS OF REALISM. BECAUSE OF THE KNOCK ON EFFECTS ON THE OTHER DEFENDANTS AND CREDITORS OF ANY INCREASE IN BA'S OFFER IT IS CLEARLY VERY DIFFICULT FOR THEM TO MAKE ANY GREAT MOVEMENT TOWARDS EXIM'S POSITION. THE PROBLEM FACING US HOWEVER IS THAT IT IS DIFFICULT FOR US TO GO BACK TO FIELDING, WALLIS OR PRICE TO ASK FOR MORE HELP WHEN EXIM HAVE MOVED BUT BA HAVE NOT. AS OF TONIGHT THE CONDITIONS DO NOT YET APPEAR TO BE THERE FOR ANY SUCCESSFUL POLITICAL INTERVENTION.

15.

5. WE HAVE DISCUSSED THE POSITION WITH PARK AND MARSHALL WHO ARE WILLING TO GO BACK TO EXIMBANK AND MAKE A SLIGHTLY IMPROVED OFFER AS SOON AS A FURTHER SUITABLE MEETING CAN BE ARRANGED. THEY AND WE AGREE THAT SUCH A MEETING SHOULD BE ON A ONE TO ONE BASIS AS BETWEEN DRAPER AND PARK (OR POSSIBLY MARSHALL) PLUS ONE ''REFEREE''. POSSIBLE NAMES FOR THE ''REFEREE'' ARE FIELDING, PRICE, VANCE MOORE (EX WHITE HOUSE COUNSEL) OR ANNENBURG. IT WOULD SEEM TO US HIGHLY DESIRABLE TO ARRANGE SUCH A MEETING FOR 4 MARCH SO THAT A FURTHER POLITICAL INTERVENTION WOULD BE POSSIBLE AFTERWARDS IF IT WERE NOT SUCCESSFUL.

6. IN THE MEANTIME YOU WILL WISH TO BE CONSIDERING HMG'S POSITION AS TO THE MAGNITUDES OF THE SETTLEMENT MONIES WHICH WOULD BE PAYABLE BY BA AS A RESULT OF NEGOTIATIONS WHICH WILL HAVE TO MOVE VERY RAPIDLY NEXT WEEK IF AGREEMENT IS TO BE REACHED BEFORE THE EXPIRY OF THE TRUCE IN THE LAW COURTS. PARK IS SEEKING AN EXTENSION OF THIS BUT SUCCESS CANNOT OF COURSE BE GUARANTEED. AND IF THE DISCOVERY PROCESS IS RESTARTED THE DAMAGE IS LIKELY TO BECOME IRREPARABLE VERY RAPIDLY.

7. I SHALL BE DISCUSSING THE FOREGOING WITH PARK AND MARSHALL AT 10 AM ON 1 MARCH AND SUBJECT TO DISCUSSION WITH THEM PROPOSE TO APPROACH FIELDING TO SUGGEST A ONE-TO-ONE MEETING BETWEEN PARK AND DRAPER ON THE AFTERNOON OF 4 MARCH WHICH FIELDING OR ANOTHER US ''REFEREE'' MIGHT ALSO ATTEND.

8. GRATEFUL FOR ANY INSTRUCTIONS DESKBY 011400Z.

9. ADVANCE COPIES TO KNIGHTON HOLMES FORTNAM DTP, BRAITHWAITE O'NEILL GRAY FCO, AUST LEGAL ADVISERS FCO, AYLING DTI, GARDINER LAW OFFICERS DEPT, HEALEY RICKFORD DTI, GREGSON CABINET OFFICE, WILSON TREASURY.

WRIGHT

(ADVANCED AS REQUESTED)

LIMITED

HD/MAED
HD/NAD
MR BRAITHWAITE
MR O'NEILL

COPIES TO:-

MR AUST LEGAL ADVISERS
MR KNIGHTON DEPT OF TRANSPORT
MR HOLMES " "
MR FORTNAM " "
MR HEALEY DTI
MR RICKFORD "
MR AYLING " , SOLICITORS
MR GARDINER LAW OFFICERS DEPT
MR GREGSON CABINET OFFICE
MR WILSON TREASURY

File
Chron F.

CONFIDENTIAL

MR REDWOOD

26 February 1985

AIRPORTS POLICY

The group of officials, recently formed to prepare the ground for a White Paper on Airports Policy and Airports Privatisation, is getting into its stride. Although Ridley's officials are concerned that he should not compromise his judicial function in considering the Eyre Report on Stansted and Heathrow T5, Ridley has been taking soundings from the various opponents of the expansion of the London airports' system with the objective of finding a politically saleable package.

That package is shaping up as follows:

- Expansion of terminal capacity at Stansted to 15 million ppa would be approved, but subject to prescribed phasing, and arrangements which ensure that the Government must obtain parliamentary endorsement before proceeding to full capacity. One idea, for example, would be to authorise the first phase of new terminal capacity at Stansted, with subsequent phases being the subject of affirmative resolutions in Parliament.

- Luton would be developed to a maximum capacity of 10 million ppa.

- T5 at Heathrow would not be approved, but the 275,000 atm limit on aircraft movements would not be imposed.

- Efforts are being made to find measures which would help to appease the regional airports lobby.

This package would have the merit of utilising a fourth full-scale international runway (Stansted) as part of the London airports' system. The likely break in the trend

towards larger aircraft carrying bigger average passenger loads, and the aim of commercial liberalisation of air transport, combine to make a compelling case for this fourth runway.

Luton airport, as currently conceived and operated, has a maximum capacity of some 5 million ppa. Expanding it to 10 million ppa as part of the package, owes more to political considerations than anything else. The runway is limited and would interfere with two military airfields. Generally, the site is cramped and surface access is difficult. It is believed that an expansion of Luton from 5-10 million ppa would entail another major public inquiry of considerable duration.

As I have argued before, the logic of a fifth terminal at Heathrow is less obvious. The question is whether the limiting factor on expansion of Heathrow's throughput will be terminal capacity or runway capacity. Terminal capacity will only become a limiting factor if the trend towards larger average passenger loads continues steadily upwards, from something of the order of 100 at present to something nearer 180 in the latter half of the 1990s. There are good technical and commercial reasons why that trend is unlikely to be sustained to this extent. The snag is that, with two runways and four terminals, Heathrow would be constrained to a maximum throughput not much in excess of 40 million ppa, ie well short of the 53 million ppa which Graham Eyre postulated in his report. The Working Group on Airports Policy is commissioning an urgent investigation into the scope for increasing Heathrow's terminal capacity by improving and streamlining the three existing terminals and T4.

I understand that Ridley intends to submit his proposed compromise formula to a small meeting of Ministers within the next week or two. He is in a dilemma. He fears that a full-blooded Eyre-type package would not be politically saleable,

especially now that his wheeling and dealing with the opponents of Stansted and Heathrow expansion have aroused expectations of a compromise solution. On the other hand he is prone to widespread criticism from those not in the special interest pressure groups to the effect that he has fudged a golden opportunity to establish UK airports policy on a sound footing. I still feel that he should aim for the latter and work at building a sufficient body of support to steer the package through.

JOHN WYBREW

Pl. file on Laker file

From the Secretary of State

12th February 1985.

Dear Margaret,

I was most concerned when Nick Ridley told us how he was trapped into seeing Laker. As I understood Nick's account he was unaware that he would be meeting Laker until he arrived at Winston Churchill's flat.

I happened to be talking to Winston recently and put it to him that he had behaved badly in trapping Nick into what might be a compromising position. He was not able to reply on the spot (others were present) but he wrote to me the next day to give his version of the matter. For your interest and out of fairness to Winston (even though on his own account he behaved recklessly) I enclose a copy of his letter.

Yours ever.

Norman

AEROSPACE; BA; Pt 3

1. On 2 Feb FHL, our near neighbour, came to dine at Broadwater following his return from the U.S.

2. A couple of days later he asked if I would arrange a meeting between him and the P.M., as he felt that things, left in the hands of lawyers, were in danger of getting out of hand. He said he was anxious to be helpful to HMG whom he felt were in danger of laying themselves open to subsequent public criticism in one or two aspects of the handling of this case) and to suggest how matters might best be resolved in such a way as to expedite the sale of BA and minimise the cost to the British taxpayer.

3. I arrange to see Ian G. in his room at the House at 3.50 pm on 6 Feb to seek his guidance. He (in my view wisely) advised it it would not be appropriate at this stage for Freddie to see the P.M. but suggested I arranged

WINSTON S. CHURCHILL, M.P.

HOUSE OF COMMONS
LONDON SWIA OAA
01-219 3405

3

a meeting for him with Nick, holding the P.M. "in reserve as a Court of Appeal".

4. I subsequently made contact with Nick, speaking with him by phone at his flat on the morning of 7 Febr. and he agreed to meet me and "my friend" at 6 pm that evening at his room.

5. I confirmed the arrangements with Freddie who, specifically to cause Nick no embarassment, asked if we could not meet at my flat so as to avoid any question being asked.

6. While appreciating Nick's discretion in not enquiring on the Departmental telephone line the identity of my "friend", when I did not see him at P.M.'s Question Time, I sought out his PPS, Angela Rumbold, and (a) told her who it was, (b) told her to tell Nick and (c) suggested she might come to be present as a witness.

7. At the start of the meeting which took place in my flat — Nick having been briefed by Angela who it was — I made very clear (and it was agreed by all concerned) that, so far as the record was concerned, this was a meeting that had never taken place.

8. Nick quite properly made clear that while he was willing to listen, he could make no comment whatever.

Whether anything has, or will, come of this meeting I do not know but I do believe that there comes a point in most litigation when it is helpful to side-track the lawyers - who have their own interests - and to have a meeting between principals. My sole interest and concern was to be helpful to the Court & to a friend.

NBPM MT 6/2 CC NO

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

The Rt Hon Michael Heseltine MP
Secretary of State for Defence
Main Building
Whitehall
LONDON SW1A 2HB

6 February 1985

Dear Michael

FALKLAND ISLANDS TROOPING CONTRACT FOR BRITISH AIRWAYS

We had a brief word last Thursday about the trooping contract to the Falkland Islands, which you agreed to place with British Airways when I raised the matter with you last summer in connection with the review of airline competition policy. Your agreement then, for which I was most grateful, was a vital element which enabled me to obtain the agreement of both British Airways and British Caledonian to the exchange of routes between them which formed the crux of our response to the CAA's recommendations.

Since then, as I explained, I have successfully persuaded British Airways to look elsewhere for the aircraft which they had assumed they would be able to lease from the RAF to use on the routes to South America they would be acquiring from BCal. They withdrew that request rather grudgingly, because I convinced them that we had not understood the use they had in mind for those aircraft. But there is no doubt that you and I agreed, and British Airways were promised, a trooping contract of the kind for which they had been invited to tender, and for which they had submitted the more attractive terms.

Having had that assurance from you, and relayed it to British Airways, I do not think we could go back on it and tell them that MOD are unwilling to honour it. The alternative proposal which your Department have made to them is not a satisfactory substitute for the work which they were led to expect, and for which they have negotiated the lease of an aircraft. Your proposal would not only be less remunerative to them, but would also leave them with spare capacity which they could not guarantee to fill on the rest of their commercial network.

The exchange of routes which was so slowly and painfully worked out in the summer has not yet been given effect by the licensing process, and if British Airways are denied their Falklands contract, it would not surprise me if they refused to keep to their part of the bargain, on the grounds that we had failed to keep ours. I was persuaded by colleagues' views last summer to limit the exchange of routes to something considerably less than the CAA had proposed, and many people felt that our response was inadequate. Our professed aims of encouraging more competition in civil aviation will hardly seem credible if we are not able to give effect to even the limited measures which we announced in September.

It is now seven weeks since I wrote to you, and British Airways are becoming increasingly concerned that your Department has still not placed the contract with them. I fear I shall not be able to calm British Airways' anxieties very much longer, so I hope I may have very early agreement from you to honour the pledge which you gave me to place this contract. You assured me that you would deal with it quickly but I thought I should write to reinforce the points I made to you orally.

I am copying this letter to the Prime Minister, to Nigel Lawson, Norman Tebbit, John Biffen and Sir Robert Armstrong.

NICHOLAS RIDLEY

CONFIDENTIAL

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

Andrew Turnbull Esq
Private Secretary
10 Downing Street
LONDON SW1

22nd January 1985

Dear Andrew,

BRITISH AIRWAYS PRIVATISATION AND US ANTI-TRUST SUITS

My Secretary of State was most grateful to the Prime Minister and other colleagues for responding so quickly to my letter of 15 January.

Peter Ricketts' letter of 17 January reported the Foreign Secretary's reservations about the wording of the last points in Sections I and II of Annex C to my Secretary of State's paper MISC(85)2 - the proposal that BA and we make clear in our public presentation of any settlement of the Laker liquidator's action that BA remain a defendant in associated class actions, in respect of which they deny liability, but which raise issues which it is desirable to resolve before privatisation is pursued.

My Secretary of State will be happy to discuss this point at today's meeting of MISC 112; but he has asked me to make it clear beforehand that it is a point to which he attaches some importance. Mr Ridley believes that, once the Laker liquidator's suit is settled, he will have to say something on the lines of what is proposed when asked - as he certainly will be by Government backbenchers and others - whether the Government now proposes to press ahead immediately with privatisation. Indeed, in order not to build false expectations, Mr Ridley is anxious to make it clear even before the Laker liquidator's suit is settled, that that alone will not be sufficient to allow privatisation to proceed immediately: the class actions will remain an obstacle for the time being.

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I am copying this letter to Len Appleyard (Foreign & Commonwealth Office), David Peretz (Chancellor's Office), Callum McCarthy (Trade & Industry), Richard Gardiner (Attorney General's Office), Helen Goodman (Financial Secretary's Office), and to Sir Robert Armstrong.

Yours,

MISS D A NICHOLS
Private Secretary

PRIME MINISTER

British Airways Privatisation and US Anti-Trust Suits
(MISC 112(85)2, 3, 4, 5 and 6)

BACKGROUND

You chaired a meeting on 17 December on British Airways (BA) privatisation and anti-trust suits. Since then, the postponement of the privatisation of BA has been announced; and Mr Ridley has obtained agreement in correspondence (his letter of 15 January) to a settlement of the civil action with the Laker liquidator if available on terms close to those in Annex A to his paper MISC 112(85)2. That paper and MISC 112(85)5 by the Financial Secretary, Treasury consider the next steps on the remaining United States (US) class anti-trust actions, their relationship to the privatisation of BA and future dealings with the United States Government on anti-trust and the Bermuda 2 agreement. MISC 112(85)6 gives the views of the Foreign and Commonwealth Secretary. MISC 112(85)3 and 4 by the Secretary of State for Transport explore in further detail some matters incidental to the main issues.

MAIN ISSUES

2. The main issues are:

i. what are the prospects for a settlement of the liquidator's action?

ii. How should BA proceed in relation to the class actions and what are the implications for privatisation?

iii. What further action should be taken and when to seek changes in US policy and/or legislation on

Bermuda 2 and the anti-trust laws?

The Liquidator's Case

3. You will want to hear the latest prospects for a settlement from Mr Ridley. His suggestions in paragraphs 15 and 16 and Annex II of MISC 112(85)2 about presentation have been generally accepted subject to comments made in correspondence, but it may be worth considering

i. can the Government, as 100 per cent shareholder in BA, maintain the complete detachment from the Board's decisions to settle proposed by Mr Ridley?

ii. Can Mr Ridley be reasonably confident that the Comptroller and Auditor General will respect BA's wish to keep the terms of the settlement secret? What might the implications be if he did not?

Anti-Trust, Bermuda 2 and Privatisation

4. Assuming that the liquidator's suit is settled, Mr Moore does not at this stage take issue with Mr Ridley's view that tactics in the next phase should be to try for an early settlement of the class actions if there is a real chance of one. BA is getting further advice bearing on this.

5. If it is not clear within a week or two what the chances are, however, Mr Ridley's and Mr Moore's views diverge. Mr Moore favours making privatisation the priority and giving a partial indemnity to allow it to proceed quickly. Problems with the US on Bermuda 2 and anti-trust should be pursued in parallel, but might have to be lived with. Mr Ridley seems prepared to wait longer for prospects in the class actions to clarify and would oppose on cost grounds an indemnity of the kind suggested by Mr Moore. He would give priority to negotiations with the US on Bermuda 2 and anti-trust, possibly including, if necessary,

notice of withdrawal from Bermuda 2; and/or what he sees as the less extreme possibility of a compensation fund financed by a ticket tax of the kind discussed in MISC 112(85)4.

6. Under Mr Ridley's proposals, privatisation would clearly take a good deal longer than under Mr Moore's, though he says he hopes it could be achieved in 1985/86. He does not appear to rule out the possibility that, in the long run, privatisation might go ahead before the class suits and negotiations with the US were over, but he proposes to choose a new target date only once decisions have been taken on

i. whether or not to threaten withdrawal from Bermuda 2 (presumably because this would have particularly major implications for the privatisation prospectus); and

ii. airports policy (on which he is due to make proposals in the next 2-3 months).

7. The Foreign and Commonwealth Secretary agrees with the Financial Secretary that the prime objective should be to neutralise the effects of anti-trust actions arising from the past. That apart, he neither supports nor rules out either Mr Moore's or Mr Ridley's approach unequivocally.

An Indemnity

8. The advantage of a partial indemnity (ie. with the Government bearing any costs in excess of some threshold amount - say $30-50 million which would remain the responsibility of BA) would be that it might allow privatisation to proceed. (The alternative option of separating BA plc from its anti-trust liabilities, discussed in MISC 112(85)3, is no longer being contemplated by the Treasury.) The disadvantages are that it would weaken BA's incentive to secure a tolerable outcome of the actions and would whet the appetite of the

but not eliminate

litigants. It would of itself increase the likely cost of resolving the suits, which might, at worst, be very significant compared with the proceeds of privatisation. The extent of the possible financial exposure is not entirely clear, but Mr Ridley mentions a theoretical maximum of $1 billion; an amount exceeding $100 million cannot be ruled out at this stage. The nature of the risk would have to be admitted at the time of privatisation and could well provide severe public and Parliamentary criticism.

Pressure on the US

9. Both Mr Moore's and Mr Ridley's approaches would have implications for relations with the US. The former could be seen as in effect accepting the application of the US anti-trust law to air services covered by the inter-Governmental agreement, since going ahead soon with privatisation would not be compatible with determined pressure on the US for a change in the situation - the action open to HMG (eg. withdrawal from the Bermuda 2 Agreement) could have a major impact on airline profitability, to which reference would have to be made in the prospectus. On the other hand, Mr Ridley's approach of political confrontation - whether through ending the Agreement or through the threat of a ticket tax - could have unpredictable and far-reaching consequences, which would require much further evaluation. A meeting under the Foreign Secretary on 6 December ruled out an indemnity in respect of the liquidator's action and expressed serious reservations about a ticket tax or other means of raising the political profile of the dispute. It may be worth pressing his representative (Mr Renton) on what course of action he would prefer if an early settlement of the class litigation seemed impossible.

Public Presentation

10. The difficulties of presenting any form of indemnity in relation to privatisation are touched on in paragraph 8 above. More generally, there would be difficulty in getting

over to public opinion why, if by reason of international agreement, US domestic anti-trust law ought not to apply to BA, it was necessary for the UK Government to pay for breaches by BA of that law rather than seek redress through legal and diplomatic channels. Moreover, Mr Ridley's compensation fund scheme, though it would remove or reduce the cost to the taxpayer of indemnifying BA, would increase costs to travellers, who are already seen in consumer circles as losers from alleged action by BA and other airlines in the Laker affair.

Next Steps

11. There are two keys to early progress. The first is a settlement with the liquidator. If that falls through, there will need to be a review of the consequences - which could be severe - for early privatisation of BA and for the Government's financial exposure if any indemnity were given. The second is the further information to be available 'in a week or two' on the prospects of an early settlement of the class actions. The Group will need to meet again to decide, in the light of this information, whether to pursue a settlement or one of the alternatives proposed by Mr Ridley and Mr Moore. It will, however, be possible now to establish whether there is any preliminary consensus on which alternative is preferable.

12. Additional work for a further meeting of the Group might be helpful on the following matters in addition to the prospects for the settlement of the class actions:

i. what are the best assessments of both theoretical and likely actual exposure of BA and the Government under a partial indemnity of the kind contemplated in MISC 112(85)5?

ii. In Mr Ridley's judgement, what is at risk in economic terms if the present Bermuda 2/anti-trust situation is allowed to continue? If the situation could be shown to inflict significant economic loss on the UK, and if there were a realistic prospect

that we could mount effective pressures on the US for a change, then there would be an argument for tackling that problem before going ahead with privatisation.

iii. What would be the options for the public presentation of the indemnity proposed by Mr Moore and the compensation scheme suggested by Mr Ridley; and what would be the likely public reaction -

a. in the UK; and

b. in the US?

13. If the Group does not rule out Mr Ridley's idea of a ticket tax, there seems no reason why the further work he suggests on it should not be done, though the suggestion that legislation should be prepared on a contingency basis seems premature.

HANDLING

14. You will want to invite Mr Ridley, Mr Moore and Mr Renton to speak on the Government's objectives and next steps. All other members of the Group will wish to contribute: you will wish to record their preliminary views on the alternative approaches suggested by Mr Ridley and Mr Moore.

CONCLUSIONS

15. You will wish to reach conclusions on the following:

i. a settlement of the liquidator's actions;

ii. with a view to a resumed discussion, further work -

a. by the Department of Transport to clarify the prospects for an early settlement of the class actions;

b. by the Department of Transport and the Treasury on the matters at paragraphs 12(i) to (iii) above.

PLG

P L GREGSON
Cabinet Office

21 January 1985

PRIME MINISTER

The Cabinet Office brief will follow on Monday. I think it will be easier to follow the paper if you read papers in the following order:-

(i) Policy Unit note

(ii) John Moore's paper - MISC 112(85)5

(iii) MISC 112(85)6

(iv) MISC 112(85)2

(v) MISC 112(85)3

(vi) MISC 112(85)4

Colleagues have agreed that a settlement with the liquidator and Sir Freddie should be sought if it can be got at or close to terms suggested. We have not yet heard result.

ANDREW TURNBULL

19 January 1985

CONFIDENTIAL

PRIME MINISTER 18 January 1985

BA PRIVATISATION AND US ANTI-TRUST

Essentially, you are offered two courses:

- the practical, which realistically focuses on our objectives (not least BA privatisation), the obstacles, and the most effective way of overcoming them;

- the affronted, which abhors the unreasonableness of the situation in which US anti-trust laws have placed us, and seeks to slay that dragon before we worry too much about the treasure.

John Moore and the Treasury want the treasure. Nicholas Ridley's instincts are first to slay the dragon. We would follow John Moore.

First, the dragon is much less dangerous than all the fire and smoke would suggest. Anti-trust as a check on the big corporations goes deep into the US business culture - back into the nineteenth century. Few large US corporations, however blue-chip and scrupulous in their behaviour, avoid anti-trust suits. Claims of billions of dollars are bandied about, but business goes on. The corporations remain credit-worthy. Their shareholders collect their dividends and sleep easy. The parasitic class action lawyers grow fat on the

system, but the out-of-court settlements are usually small in relation to the scale of business being conducted.

Against that background, our comments on Nicholas Ridley's proposals are as follows:

a) Accept proposed settlement of the liquidator's action.

We agree. It looks as if the the negotiation has reached the "moment juste", and cannot be bettered. Moreover, the settlement will reduce BA's exposure to class actions.

b) Note that BA will be exploring the possibility of settling the class actions ("normally no hope of concluding a settlement within 6-9 months at minimum").

Transport seem to be exaggerating the size of this obstacle, perhaps because they would rather be tackling the dragon.

BA have explored. Their expert lawyers (Linklater and Paine in the UK, and Sullivan and Cromwell in the US) have exhaustively reviewed BA's potential exposure to the class actions. They estimate that BA's maximum liability is of the order of $10 million. It looks as if BA will be able to insure against the outside chance of it

exceeding this figure. If not, we still have the Treasury's partial indemnity proposals as a sensible fall-back.

c) Vis à vis the US Government, to maintain your firm opposition to international aviation falling under US anti-trust laws.

Fine; right is certainly on our side, but changing the sytem will probably take a long time. It is deep-rooted. Meanwhile, a resolutely-pursued strategy is likely to be more effective than provocative tactics.

d) Agree that officials should analyse further the proposal for a compensation fund and work up legislation.

We would see this as just such a provocative tactic, which probably sacrifices BA privatisation and may ultimately hinder the removal of US anti-trust from international civil aviation.

e) Postpone a decision on the timing of BA privatisation.

Transport are right in not wanting to be publicly committed to a specific deadline until the major obstacles have been overcome. However, without setbacks on the Laker settlement and the class actions, the launch

could still be as early as July 1985. Transport should continue working on the other outstanding issues so as to keep the July option open.

f) Public Stance.

The substance looks about right, but the tone could be lighter and more positive. Making heavy weather of the anti-trust problems will not help our cause in settling the class actions, or in our public presentation here.

JOHN WYBREW

131/1

Foreign and Commonwealth Office

London SW1A 2AH

17 January 1985

Dear Dinah,

Laker: Settlement of Laker Liquidator's Suit

The Foreign Secretary has seen the paper (MISC 112(85)2) which Mr Ridley has circulated for the meeting of MISC 112 on Tuesday 22 January, and has considered the terms of the prospective settlement which British Airways would like to make with the Laker liquidator set out in Annex A of the paper, about which you wrote to Andrew Turnbull on 15 January.

Sir Geoffrey Howe agrees with the proposal in paragraphs 2 and 3 of Mr Ridley's paper that, if the final settlement terms do not differ substantially from those given in Annex A, Mr Ridley should in the circumstances endorse British Airways' intention to settle the Laker liquidator's suit. The Foreign Secretary has reservations, however, about the wording of the last points in Sections I and II of Annex C to Mr Ridley's paper. He does not think it is in our interests to put it so publicly on record that privatisation depends on settling the class action, since this tends to play into the hands of the class actions lawyers. He thinks that Annex C deserves further consideration.

The Foreign Secretary understands that, even with settlement of the liquidator's action, BA cannot be privatised until the class action is disposed of, while the existence of the class action means that there is also a significant danger of the disclosure of British Airways documents damaging British Airways and British Caledonian. He therefore hopes that no effort will be spared to encourage British Airways to settle that action too as soon as possible.

/I am

I am copying this letter to Andrew Turnbull and to the other recipients of your letter.

Yours ever,

Peter Ricketts

(P F Ricketts)
Private Secretary

Miss Dinah Nicholls
PS/Secretary of State
Department of Transport
2 Marsham Street
LONDON SW1

NBAT

AT 17/1

01-405 7641 Ext. 3040
3229
Communications on this subject should be addressed to
THE LEGAL SECRETARY
ATTORNEY GENERAL'S CHAMBERS

ATTORNEY GENERAL'S CHAMBERS,
LAW OFFICERS' DEPARTMENT,
ROYAL COURTS OF JUSTICE,
LONDON, W.C.2.

17 January, 1985

Dear Miss Nichols,

BRITISH AIRWAYS PRIVATISATION AND US ANTI-TRUST SUITS

1. I refer to your letter of 15 January to Turnbull in which you ask for an indication of the views of Ministers on the proposed settlement of the Laker Liquidator's action against British Airways and others.

2. The Attorney General considers that it would be eminently sensible to settle on the terms described in MISC 112(85)2 if these can be achieved.

3. Even were it possible to be confident that the Liquidator's action could be successfully defended in a system which is so heavily loaded against defendants, there is every reason to believe that the procedure of discovery of documents in the USA in this case will lead to disclosures which would result in further US cases with alarmingly large potential liabilities. The longer this action runs the larger the risks associated with it.

4. The Attorney General shares the distaste felt for the proposed payment to Sir Freddie Laker; but paying him a sum that is small compared with what he might otherwise win is a necessary part of the price to be paid for the certainty achieved by buying off the trouble he might cause and the high risk of escalation.

5. Accordingly, the Attorney General agrees that British Airways should be given every possible private encouragement to settle though he also agrees that this is ultimately a matter within the responsibility of the Directors and should therefore be publicly acknowledged by HMG only to the extent and in the manner described in Annex C II to MISC 112(85)2.

6. I am copying this to the Private Secretaries to the Prime Minister, the Secretary of State for Foreign and Commonwealth Affairs, the Chancellor of the Exchequer, the Secretary of State for Trade and Industry, the Financial Secretary to the Treasury and Sir Robert Armstrong.

Yours sincerely,
Richard Gardiner
R K GARDINER

Miss D A Nichols
Private Secretary to the Secretary of State for Transport
Department of Transport
2 Marsham Street
London SW1

CONFIDENTIAL

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CC NO

Foreign and Commonwealth Office

London SW1A 2AH

17 January 1985

Dear Dinah,

Laker: Settlement of Laker Liquidator's Suit

The Foreign Secretary has seen the paper (MISC 112(85)2) which Mr Ridley has circulated for the meeting of MISC 112 on Tuesday 22 January, and has considered the terms of the prospective settlement which British Airways would like to make with the Laker liquidator set out in Annex A of the paper, about which you wrote to Andrew Turnbull on 15 January.

Sir Geoffrey Howe agrees with the proposal in paragraphs 2 and 3 of Mr Ridley's paper that, if the final settlement terms do not differ substantially from those given in Annex A, Mr Ridley should in the circumstances endorse British Airways' intention to settle the Laker liquidator's suit. The Foreign Secretary has reservations, however, about the wording of the last points in Sections I and II of Annex C to Mr Ridley's paper. He does not think it is in our interests to put it so publicly on record that privatisation depends on settling the class action, since this tends to play into the hands of the class actions lawyers. He thinks that Annex C deserves further consideration.

The Foreign Secretary understands that, even with settlement of the liquidator's action, BA cannot be privatised until the class action is disposed of, while the existence of the class action means that there is also a significant danger of the disclosure of British Airways documents damaging British Airways and British Caledonian. He therefore hopes that no effort will be spared to encourage British Airways to settle that action too as soon as possible.

/I am

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I am copying this letter to Andrew Turnbull and to the other recipients of your letter.

Yours ever,

Peter Ricketts

(P F Ricketts)
Private Secretary

Miss Dinah Nicholls
PS/Secretary of State
Department of Transport
2 Marsham Street
LONDON SW1

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FILE

Rey

10 DOWNING STREET

From the Private Secretary

17 January, 1985

Dear Diral.

BRITISH AIRWAYS PRIVATISATION AND US ANTI-TRUST SUITS

The Prime Minister has seen your letter to me of 15 January and Frances Bogan's letter to you of 16 January. She agrees that if a settlement with the liquidator and Sir Freddie Laker personally could be reached on terms close to those set out in Annex A of MISC 112 (85)2), BA should be authorised to accept it. The Prime Minister has noted the points made by the Financial Secretary and hopes that care will be taken in justifying the payments to Sir Freddie Laker personally and to his lawyers.

I am sending a copy of this letter to Len Appleyard (Foreign and Commonwealth Office), Rachel Lomax (HM Treasury), Callum McCarthy (Department of Trade and Industry), Richard Gardiner (Attorney General's Office), Helen Goodman (Financial Secretary's Office) and to Richard Hatfield (Cabinet Office).

Yours sincerely

Andrew Turnbull

(Andrew Turnbull)

Miss D. Nichols,
Department of Transport

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E.R.

File

PRIME MINISTER

MISC 112 will discuss BA privatisation/Laker/US anti trust suits next week. Mr. Ridley seeks to bring forward agreement on one element in this complex - the settlement with the liquidator - paras. 1-3 and Annex A of the attached paper.

If, as suggested, a settlement is available at $50 million for all airlines and $20 million for BA, John Redwood and I advise acceptance. The Treasury agree, though they wish to be sure that the payments to Sir Freddie Laker personally and to his US lawyers, $8 million each, are entirely above board.

Agree?

16 January 1985

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FINANCIAL SECRETARY TO THE TREASURY

Treasury Chambers, Parliament Street, SW1P 3AG

Miss D A Nichols
Private Secretary to
Secretary of State for Transport
Department of Transport
2 Marsham Street
LONDON
SW1P 3EB

16 January 1985

Dear Dinah

BRITISH AIRWAYS PRIVATISATION AND US ANTI-TRUST SUITS

With AT?

The Financial Secretary has seen your letter of 15 January to Andrew Turnbull. He agrees that the Government should not stand in the way of a settlement of the Laker liquidator's action broadly on the terms indicated in Annex A to MISC 112(85)2. He has commented however that the payments to Laker (and to a lesser extent Beckman) will be potentially awkward to explain. He has also noted that it will be important that BA's actions are beyond reproach as far as any suggestions of tax avoidance are concerned.

With AT?

I am copying this letter to Andrew Turnbull, Len Appleyard (Foreign and Commonwealth Office), David Peretz (Chancellor's Office), Callum McCarthy (Trade and Industry), Richard Gardiner (Attorney General's Ofice), and to Sir Robert Armstrong.

yours sincerely
FP Bogan

MISS F P BOGAN
Assistant Private Secretary

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

Andrew Turnbull Esq
Private Secretary
10 Downing Street
LONDON SW1

15th January 1985

Dear Andrew,

BRITISH AIRWAYS PRIVATISATION AND US ANTI-TRUST SUITS

My Secretary of State is today circulating three papers for the meeting of MISC 112 on Tuesday 22 January. One of these (MISC 112(85)2) describes the next steps Mr Ridley proposes should be taken over this problem; in particular it outlines the terms of the settlement of the Laker liquidator's action which BA are hoping to conclude very shortly, and seeks colleagues' agreement that British Airways' decision to settle broadly on these terms should be endorsed.

We have just heard that the British Airways Board is to meet tomorrow (Wednesday) to consider the terms of settlement which are emerging, and is likely to approve them. If the Board approves settlement British Airways and its negotiators will then wish to proceed with all speed to conclude the negotiations and to complete the documentation. To this end British Airways would find it very useful to have by Thursday 17 January an indication of the Government's willingness to acquiesce in what is proposed.

My Secretary of State wishes to give British Airways every possible assistance in this matter. As the paper explains, he believes that he should endorse the terms on which BA propose to settle, and he shares British Airways' concern over the dangers of any delay. He would therefore be most grateful for an indication by 5 pm on Thursday of the Prime Minister's and other colleagues' views of this aspect of his paper.

I am copying this letter to Len Appleyard (Foreign & Commonwealth Office), David Peretz (Chancellor's Office), Callum McCarthy (Trade & Industry), Richard Gardiner (Attorney General's Office), Helen Goodman (Financial Secretary's Office), and to Sir Robert Armstrong.

Yours,

Dinah

MISS D A NICHOLS
Private Secretary

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NOPM AT 14/1

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

Andrew Turnbull Esq
Private Secretary
10 Downing Street
LONDON SW1

14 January 1985

Dear Andrew,

US ANTI-TRUST SUITS

I am so sorry that the note from the British Embassy in Washington to the Department of State of 6 May 1983, referred to in the draft reply for the Prime Minister to send to Ambassador Price, was accidentally omitted from my letter circulated earlier today. I attach a copy.

I am copying this to Len Appleyard (Foreign & Commonwealth Office), Callum McCarthy (Trade & Industry), and Henry Steele (Attorney General's Office).

Yours,

Dinah.

MISS D A NICHOLS
Private Secretary

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GRS 200

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DESKBY BOTH 111715Z
FROM UKMIS NEW YORK 111606Z JAN 85
TO IMMEDIATE FOREIGN AND COMMONWEALTH OFFICE
TELEGRAM NUMBER 16 OF 11 JANUARY
AND TO DTI

DTI FOR R J AYLING DTI SOLICITORS

LAKER

1. FOLLOWING MESSAGE RECEIVED THIS MORNING FROM PARK AND BRISTER FOR ONWARD TRANSMISSION TO AYLING:

''UPDATE ON CONTRIBUTORS

BA	20 MILLION DOLLARS
PAN AM	10 MILLION DOLLARS PLUS AIRBUS) MORE INFORMATION
TWA	8 - 10 MILLION DOLLARS) LATER TODAY
B CAL	5 - 7 MILLION DOLLARS
EUROPEANS	10 - 15 MILLION DOLLARS (NOT GOOD ENOUGH)
UTA	NIL

PAYMENTS: CURRENT TARGET

MITSUI	0.25 MILLION DOLLARS
GENERAL ELECTRIC	0.25 MILLION DOLLARS
AIRBUS	0.25 MILLION DOLLARS - BALANCE COURTESY OF PAN AM
EXIM	0.25 - 1 MILLION DOLLARS
MCDONNELL DOUGLAS	NIL
MIDLAND/CLYDESDALE	NIL
F LAKER	10.0 MILLION DOLLARS
BECKMAN	10.0 MILLION DOLLARS
AIR TRAVEL RESERVE FUND	1.75 MILLION DOLLARS (MAYBE 2.50 MILLION DOLLARS)
TRADE CREDITORS	9.30 MILLION DOLLARS
CONTINGENCIES	5.0 MILLION DOLLARS

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AS TO EUROPEANS, WE MIGHT TARGET FOR 12.5 MILLION DOLLARS PLUS 2.5 MILLION DOLLARS OF B CAL CONTRIBUTION, IE 15 MILLION DOLLARS TOTAL FOR REFINANCING CONSPIRACY.
HAVE ARRANGED FOR SCHEDULE OF UPDATED ANALYSIS OF CREDITORS TO BE SENT BY HAND FROM OUR LONDON OFFICE. THIS SETS OUT OUR BEST CURRENT INFORMATION.''

2. FCO PLEASE ADVANCE TO BRAITHWAITE, DUSS.

MAXEY

[ADVANCED AS REQUESTED]

US ANTI-TRUST ACTION AGAINST BRITISH AIRLINES

LIMITED

MAED
NAD
NEWS D
ERD
PLANNING STAFF
LEGAL ADVISERS
PS
PS/MR RIFKIND
PS/MR RENTON
PS/PUS
MR BRAITHWAITE
MR O'NEILL
MR DAVID THOMAS

ADDITIONAL DISTRIBUTION
US ANTI-TRUST ACTION AGAINST BRITISH AIRLINES

CONFIDENTIAL

File ~~MISC 112 folder~~

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

Andrew Turnbull Esq
Private Secretary
10 Downing Street
LONDON SW1

8 January 1985

Dear Andrew,

BRITISH AIRWAYS PRIVATISATION

As you are aware, the Government has not yet publicly announced the deferral of the privatisation of British Airways, but it is likely that questions will be tabled when the House resumes. My Secretary of State proposes that any reply should be as follows:

> "I have decided reluctantly that the privatisation of British Airways must be deferred. It remains our firm intention, however, to proceed with privatisation as soon as practicable in the next financial year. It is desirable to resolve some of the uncertainties created by the application of US anti-trust law. A delay should also assist BA's balance sheet through the accumulation of profits, and should reduce the need for a capital injection by the Government."

The text has already been discussed between officials. My Secretary of State is aware that it has been suggested that the last sentence should be omitted. He considers, however, that it should remain, particularly to counter press speculation that a large capital injection by the Government will bw needed when BA is privatised.

Mr Ridley would be grateful to know as soon as possible whether the text is acceptable. He does not think that at this stage it is necessary for the Government to initiate the announcement, either by a Parliamentary statement or by an arranged Parliamentary question, but he will of course keep the position under review in the lights of developments in negotiations on the Laker anti trust suits and of comments in the press.

I am copying this to the Private Secretaries to the Foreign & Commonwealth Secretary, the Chancellor of the Exchequer, the Lord Privy Seal, the Secretary of State for Trade & Industry, the Attorney General, the Financial Secretary, the Chief Whip and to Sir Robert Armstrong.

Yours,

Diana

MISS D A NICHOLS
Private Secretary

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

7 January 1985

Miss D A Nichols
Private Secretary to the
Secretary of State for Transport

Dear Diana

BRITISH AIRWAYS: LAKER LIQUIDATOR'S SUIT

The Chancellor saw and noted the contents of your letter to me of 21 December. He has also noted the Prime Minister's comment recorded in David Barclay's letter of 31 December.

The Chancellor would be grateful to continue to be kept in touch with progress on arranging a settlement. He also looks forward to receiving soon the paper on ways of divorcing the BA flotation from the anti-trust issues which it was agreed would be produced in consultation with the Treasury.

On public presentation the Chancellor noted from the penultimate paragraph of your letter, that you are preparing a press announcement of a substantial deferment of privatisation. He is concerned that no such briefing or statement should be made without his prior agreement. Our two offices have already spoken about this.

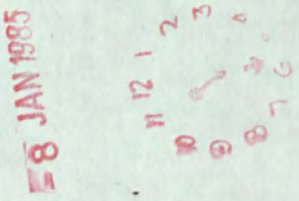
I am copying this letter to Andrew Turnbull (No.10), Len Appleyard (FCO), Henry Steel (Law Officers Dept.), Callum McCarthy (DTI) and Richard Hatfield (Cabinet Office).

Yours ever
David

D L C PERETZ
Principal Private Secretary

AEROSPACE: Future of BA

B 3



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FILE

VC

B/c: P. Coggan
J. Wybrew.

10 DOWNING STREET

From the Private Secretary

4 January 1985

Dear Diana,

PRIME MINISTER'S MEETING WITH THE SECRETARY OF STATE FOR TRANSPORT

Your Secretary of State came to see the Prime Minister yesterday to report on the various policy questions facing his Department.

On buses, he said the Bill would not be published until the end of January. It was likely to be very long and very contentious, with strong opposition coming particularly from urban areas. Nevertheless he was sure it could be got through. The Prime Minister urged him to organise a group of backbench supporters. Your Secretary of State said such arrangements were in hand.

On airports policy, your Secretary of State said the CAA Bill would have to be put into abeyance for the time being. It was desirable to have the debate on the Eyre Report as soon as possible, possibly in the first week of February, with detailed Ministerial consideration to begin immediately afterwards. He believed the right course was for the Government to prepare a comprehensive statement on all aspects of airports policy - the response to the Eyre Report, the response to the review of Scottish airports, and the Government's intentions on privatisation/injection of private capital into the aiports of BAA and the local authorities. As a preparatory step, he was proposing to create a number of separate PLCs, one for the three London airports, one for the two lowland Scottish airports and separate ones for the rest. He hoped such a document could be prepared by May or June. It might be better to let the present CAA Bill lapse and to introduce a more comprehensive bill in the next session dealing with all these questions. He would want to include in such a bill a power to limit movements into Heathrow as this was necessary to safeguard smaller UK airlines from powerful overseas operators. The Prime Minister was content with this approach.

Your Secretary of State said that in addition to the Essex/Cambridge group of MPs opposed to Stansted there was a powerful group of Government backbenchers supporting the development of Manchester. To secure their support it would be necessary to devise ways of securing additional traffic through Manchester.

Discussion then turned to the problems of BA privatisation, the Laker liquidators and the US anti-trust suits. The Prime Minister gave an account of her discussions with President Reagan. She had told him that, while the US favoured liberalisation, the effect of its treble damage legislation was to frustrate the Government's most important initiative for liberalisation and de-nationalisation. Although it was possible to achieve agreements on lower fares under the Bermuda 2 Agreement procedures took several months. She had also said that while the US favoured greater competition it had 65% of the Atlantic traffic and a virtual monopoly of the feeder traffic within the US. She felt that the Bermuda 2 Agreement had become unworkable and that a new framework was required.

Your Secretary of State reported on the position reached with the Laker liquidator. Although there was a reasonable chance of agreeing a global sum with him, it was proving difficult to agree an allocation between the different airlines which was fair to BA. Even if a solution were found, there was still the possibility that Sir Freddie Laker might take legal action personally. On top of that there was the prospect of still further anti-trust actions. All this was making it very difficult to see how the privatisation of BA could be achieved. The Prime Minister thought there was no point in settling with the liquidator if that made it easier for Laker himself to bring separate actions.

The Prime Minister asked whether the creation of a new BA PLC, leaving the legal liabilities with a shell company could help. Your Secretary of State said that if the effect was to limit the ability of US claimants to collect damages which they had been awarded, US Courts might allow BA's assets in the US, ie its planes, to be impounded.

He was still strongly opposed to an indemnity although BA were pressing strongly for this. He thought it might be necessary to consider ways of exerting more pressure on the US eg by a declaration that any damages awarded would not be paid or through the threat of a ticket tax to recoup the cost of any such damages. It was agreed that these issues would need to be discussed soon in the Ministerial group being set up by the Cabinet Office.

Yours sincerely

Andrew Turnbull

ANDREW TURNBULL

Miss Dinah Nichols,
Department of Transport.

NANCIAL TIMES

THURSDAY JANUARY 3, 1985

1

BA PRIVATISATION PLANS

A rare game of poker

By Duncan Campbell-Smith

10

HAMPAGNE corks were already set to pop at the end of November, as the ɔtation of British Telecom ɔvered on the brink of final ıccess. No one that week ɜard the impact on the overnment's privatisation proɔramme of a different kind of ıng altogether.

A small bomb had in fact ɔne off under British Airways. arrived at the offices of Hill amuel, the merchant bank, dvising the Department of ransport on its sale of the airne, and it came wrapped in BA envelope.

The contents of that envelope ffectively killed the chances of BA flotation stone dead for ıe current financial year. And ıey triggered a period of renetic activity, suspended for hristmas and now just getting nder way again, on which ıust hang the prospects of BA eaching the private sector at ll in the foreseeable future.

Hill Samuel had been asking BA's top executives for months ɔast to address a most uncomortable question. Mr Christoɔher Morris, the liquidator of Laker Airways, was pushing teadily ahead with a claim in he U.S. courts for damages ıgainst BA of more than $1bn. What reassurance could BA ɔffer prospective shareholders hat this contingent liability would never have to be met?

The airline's report and ıccounts published last June ıad airily dismissed Mr Morris's claim as "unfounded" in the briefest of footnotes to the balance sheet. Hill Samuel had quickly made clear that this was well short of a satisfactory response. But attempts to elicit something more substantial met with no success at all through the autumn.

It might be rash to construe this as deliberately evasive action on BA's part. On the one hand, it was more than a little pre-occupied until early October with a furious lobbying campaign against the July report of the Civil Aviation Authority urging the transfer of some BA routes to the independent airlines. On the other, it had reason to hope its legal difficulties in the U.S. would eventually be resolved with a helping hand from the Government at the very highest levels.

Still, BA's board does appear to have been excessively optimistic. It saw off the CAA report. It watched the Government prevail on President Reagan to scotch criminal action against it in the U.S. on anti-trust grounds. But by late November, Mr Morris was just as real a threat as he had always been. It was time, said Hill Samuel, for BA to put together a formal draft of what the sale prospectus might tell nervous investors about that billion dollar claim.

BA naturally turned to its U.S. counsel for the job. It requested a draft notice of the claim which would provide as much comfort as was compatible with a fair and truthful summary of the outlook for Mr Morris's suit. What it got back from New York was a thousand words which emphatically did not add up to "unfounded."

Round went the opinion of Messrs Paul, Weiss, Rifkind, Wharton and Garrison to Hill Samuel at the end of November. The detonation was immediate. BA, said the bankers, would be unmarketable if the opinion were included in the prospectus—and unmarketable if it were not.

All three of the main parties to the BA sale—the financial advisers, Whitehall and BA itself—have adjusted to this extraordinary setback with remarkable discretion. Behind the scenes, though, their reactions have differed in subtle and revealing ways.

For the advisers, and especially Hill Samuel, it has entailed a good deal of frustration. Weekly drafting meetings since the middle of October had produced an almost completed prospectus by the beginning of December, accompanied by a U.S. registration document in case the decision were taken to float BA on both sides of the Atlantic simultaneously.

These documents only awaited the insertion of BA's pre-privatisation balance sheet: a delicate matter, admittedly, but not an inordinately complex one. As a result of the delay—which means that BA's privatisation will now have to come after the Budget—the sale prospectus will have to include the audited results for the year to next March 31. And if there is any delay much beyond the publication of these results; a profit forecast for 1985-86 will also be required.

In a more general sense, the frustration of the City advisers can also be attributed to their sudden sense of impotence. Having already endured a two-month delay in August-September for the political row over the CAA report, they have now to sit on the sidelines once again. At a time when the advisers might have been hoping to settle final decisions such as the method of sale and the breadth of the marketing campaign, they must await the outcome of a legal conundrum which has left them as much in the dark as almost everyone else.

Whitehall's reactions look much more complicated. Obviously, since an immediate goal of Government policy had been made much less accessible, the Laker factor could hardly be seen as encouraging. But news of the legal problem seems to have caused less than widespread dismay.

Indeed, it is easy to imagine the faintest smile gliding across more than a few Whitehall faces. Lord King, the chairman of BA, has consistently used his own skills as a publicist to upstage the more traditional deliberations of the civil service: by temperament, he seems inclined to seek de facto acceptance of his initiatives by pushing them ahead as publicly as possible, outflanking Whitehall's objections in the process.

> Relations between the BA board and the civil servants in charge of its sale have undoubtedly been under strain

BA seems to have used this approach in encouraging expectations that mid-February had been set as the target date for its privatisation. Neither the Treasury nor the Department of Transport appear to have been happy with such a precise schedule—which first emerged publicly at the start of November—and the collapse of Lord King's timetable probably caused some private satisfaction in both ministries.

As this might suggest, relations between the board of BA and the civil servants in charge of its sale have undoubtedly been under strain. The ebullience of Lord King and some of his colleagues has underlined the contrast evident in the tactical approach of the two sides. But there have been deeper causes of friction, too—and, here again, Whitehall might regard the legal delay with rather mixed feelings.

It is clear that in the exchanges of the last few months over BA's capital structure, the airline has not been averse to trying to twist the arm of Mr Nicholas Ridley, the Minister of Transport, on a number of subsidiary issues. BA is seeking, for example, to minimise the possibility that it might be asked to move some of its services to Stansted airport by arguing that this could add £150m to its future cash needs.

Similarly, BA is insisting that the Government raise its traffic capacity ceiling for ... row Airport. If it does ... says the airline, then wider-... aircraft will have to be ... to the BA fleet. And this could add 50-60 per cent to the capital expenditure projections which the City has been assuming until now for 1985-86 and 1986-87.

Against this background, the extension of the flotation schedule has the obvious disadvantage for the Government that a few more months will be available for squabbles over

CONT...

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these and other subordinate issues which might be damaging to the main task in hand. By the same token, however, the delay may have given the Treasury a welcome respite to appraise BA's own assessment of its balance sheet requirements—with less pressure to reach immediate agreement.

Lord King delivered that assessment ostensibly with every confidence that immediate agreement was hardly more than a formality. If 100 per cent of BA were to be sold for £1bn, he wrote to Mr Ridley on October 31, then it was his happy privilege to be able to tell the Minister that the Government could look forward to retaining more than 50 per cent of the proceeds.

Thanks; but no thanks, was the essence of the Treasury's reply to that. Towards the end of November, at a formal meeting between the two sides, the Treasury indicated that—far from injecting £400m or more of the proceeds back into BA, as Lord King had in mind, to help push debt well under 50 per cent of shareholders' funds—it envisaged a £100m injection as a realistic maximum.

Lord King and his board were invited to go away and work out all the implications of that. After five days juggling its October 31 figures, BA replied uncompromisingly. The £100m plan, said the airline, would force it to cut another 5,000 jobs and sell off a whole category of airplanes. . . .

But by the time this dire prognosis hit the Minister's desk, BA was already engulfed in the consequences of that opinion from its U.S. counsel on the pending Laker suit.

What, finally, has been BA's own reaction to the legal setback?

It is not the first difficulty encountered by Lord King's board. Its early decision not to contemplate shareholders' perks, for example, encountered some private criticism in the light of BT's experience—and the Department of Transport has clearly had second thoughts about BA's initial preference for a preponderance of institutional shareholders. Again, the airline's express wish to leave the privatisation advertising campaign to its own agency, the Dorlands subsidiary of Saatchi and Saatchi, has been rejected by the Government and its advisers. The mandate has gone to Allen Brady and Marsh, a rival agency.

But none of these issues, sometimes to Whitehall's consternation, have had any conspicuous effect on the self-assertiveness of the company's directors. The striking thing, indeed, is how fast and how adroitly they have adjusted to adversities big and small on the road to privatisation. And their response to the Laker liquidator's threat has proved no exception.

Within a matter of days at the start of last month, talks were under way to strike an out of court settlement with Mr Morris. Lord King summoned all his colleagues to BA's St. James's Square headquarters on December 14 and told them the news: a deal would be struck.

When and how, of course, remains another matter. The talks have proceeded in great secrecy, with Mr Morris himself in purdah for weeks past. Since BA is only one of 12 defendants being sued by the liquidator, the first task was to establish that all 12 were disposed to settle, on the right terms.

BA evidently wasted no time making clear that it would go it alone if necessary. It was quickly agreed to seek an all-in-one package.

An expert team of solicitors led by the City firm Linklaters and Paines was assigned to the work of negotiating that package with Mr Morris, while BA inevitably found itself left with the role of co-ordinator between the lawyers and the other co-defendants.

The optimists are hoping for a successful outcome before the end of this month. They can point to the fact that 85 per cent of civil anti-trust suits such as this one are settled out of court in the U.S. And Mr Morris may have to prove himself a gambler of steely nerve if he is going to sit it out for much longer in this company with the hope of a higher payoff.

But he retains three powerful cards in his hand, whatever the legal merits of his case. He knows the UK Government is keen to avoid further public battles between U.S. anti-trust principles and the time-honoured regulation of the North Atlantic air routes. He knows BA is anxious to forestall the additional disclosures which might be required of it by any long-running U.S. court action. And he knows that a settlement is now seen as virtually a *sine qua non* of any BA departure for the private sector this year. It looks a rare game of poker.

THE Sun

LOST JET HUNT 2

U.S. and Bolivian planes have found no trace of an Eastern Airlines jet missing in the Andes with 33 people aboard.

Daily Telegraph

PLANE WRECK 'SIGHTED'

By Our New York Staff

Wreckage of an Eastern Airlines Boeing 727 that disappeared on Tuesday on a flight from Asuncion, Paraguay, La Paz, Bolivia, was reported sighted yesterday in mountainous terrain 50 miles east-south-east of its destination.

But the airline said it was still awaiting conformation. Among the 33 passengers was Mrs Marian Davis, wife of the American Ambassador to Paraguay. There was high-level fog at the time.

THE GUARDIAN

Airliner wreckage sighted 4

A BOLIVIAN pilot said yesterday he had sighted wreckage of a plane in the Andes near where a US Eastern Airlines airliner with 35 people aboard disappeared on Tuesday night.

The pilot of the Lloyd Aereo Boliviano airliner said he saw the wreckage on the 21,450-foot Illimani Peak which overlooks La Paz.

In Asuncion, the US embassy said Mrs Mariam Davis, wife of the US ambassador to Paraguay, and Mr William Keely, head of the American Peace Corps in the country, were among those on board the US Plane. — Reuter.

5/2

10 DOWNING STREET

AT.

These are all the loose papers concerning civil aviation. Please advise which papers are to be included and whether any others are needed.

Julie

2.1.85.

E.R.

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PRIME MINISTER

Meeting with Mr. Ridley

i) Buses Policy

Mr. Ridley is attempting a major restructuring of the bus industry. In my view Parliament and the outside world have been slow to realise the full extent of his proposals but realisation of this is now beginning to dawn. As well as predictable opposition from transport unions and urban transport authorities, mainly Labour controlled, there will be certainly apprehension and possibly also strong opposition from the counties which will be taken up by Tory backbenchers. Mr. Ridley wants to put you in the picture of the difficulties ahead.

ii) Civil Aviation Bill/Stansted/Heathrow

Mr. Ridley will be interested to learn of your reactions to the Eyre Report. He can bring you up-to-date on the future of the Civil Aviation Bill.

iii) BA Privatisation/Laker Liquidator/US Anti-Trust Suits

Mr. Ridley has seen the record of your discussion in Washington but will nevertheless welcome a report from you directly. You have seen a report on the discussions with the Laker liquidator. Mr. Ridley will be able to bring up up-to-date if there have been any further developments.

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iv) Airports Policy

The development of policy at airports has been held back by the attention given to the CAA review, the privatisation of BA and now Stansted. Nevertheless, Mr. Ridley still wishes to make progress towards privatisation and the introduction of private capital.

2 January 1985

CONFIDENTIAL

10 DOWNING STREET

From the Private Secretary

31 December 1984

British Airways: Laker Liquidator's Suit

The Prime Minister has seen a copy of your letter of 21 December to David Peretz, reporting on the latest negotiations between British Airways and the Laker Liquidator.

The Prime Minister has noted the position. She agrees with your Secretary of State that the possible settlement which may now be emerging is far from satisfactory. She would be grateful to be kept in touch with progress.

I am sending copies of this letter to David Peretz (HM Treasury), Len Appleyard (FCO), Henry Steel (Law Officers' Department), Callum McCarthy (Department of Trade & Industry) and Richard Hatfield (Cabinet Office).

David Barclay

Miss D.A. Nichols,
Department of Transport.

KLE

RW

MR WYBREW

AIRPORT INQUIRIES 1982-83 - INSPECTOR'S REPORT

The Prime Minister did indeed read through Mr. Eyre's report over the Christmas break. She found your guidance note extremely helpful, and you may like to have the enclosed photocopy which indicates the points which she found particularly significant.

I am also returning your copies of 3 volumes of the report.

(D. Barclay)

31 December, 1984

10 DOWNING STREET

From the Private Secretary

24 December, 1984.

Dear Colin,

Civil Aviation: Laker Airways

I enclose a copy of President Regan's letter to the Prime Minister on this subject. It was seen by the Prime Minister in Washington shortly before her meeting with the President, and the text telegraphed to you.

I should be grateful for a draft reply in due course. This should take account of the points made by the Prime Minister in her discussion with the President, a record of which will reach you shortly.

It will of course be for the Department of Transport to take the lead in drafting a reply. I am therefore copying this letter and enclosure to Dinah Nichols (Department of Transport), as well as to Callum McCarthy (Department of Trade and Industry), David Peretz (HM Treasury), Henry Steel (Law Officers' Department), and Richard Hatfield (Cabinet Office).

Yours ever,

Charles Powell

Charles Powell

C.R. Budd, Esq.,
Foreign and Commonwealth Office.

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MR HATFIELD
Cabinet Office

Handling of certain civil aviation matters

The Prime Minister has now seen Sir Robert Armstrong's minute of 21 December proposing a new Ministerial Group on Civil Aviation in the MISC series. She has agreed Sir Robert's proposal on the establishment of such a group and on its terms of reference; she has however indicated that she would prefer that the normal assumption should be that she would chair the meetings.

Timothy Flesher

24 December 1984

TVF

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Ref. A084/3458

PRIME MINISTER

Handling of certain civil aviation matters

You will recall that at your meeting on 17 December to discuss the privatisation of British Airways and the anti-trust problems in the United States, certain further work was commissioned and the desire was expressed that there should be some new regular machinery for dealing with these issues. Up to now there have been ad hoc meetings of various kinds, some under the chairmanship of the Foreign and Commonwealth Secretary. This latter arrangement has not been ideal (and the Foreign and Commonwealth Office themselves share this view) for discussing the more domestic issues relating to the BA privatisation.

2. I suggest that the right way to handle these matters from now on would be to set up a new Ministerial Group on Civil Aviation in the MISC series with the following terms of reference:

> "To consider matters relating to the privatisation of British Airways, with special reference to the problems created by the United States anti-trust actions, and to consider the handling of discussions with the United States Government on civil aviation and anti-trust issues."

3. Although there may be some meetings of such a Group which you would want to chair yourself, there will be others dealing

with matters of detail and the preliminary examination of options in which you need not be involved. I therefore suggest that the regular chairman should be the Chancellor of the Exchequer, but with the explicit understanding, as in the case of the Ministerial Group on Civil Service Pay Negotiations (MISC 66), that you may wish to take the chair at particular meetings.

4. I suggest that the composition might therefore be as follows:

Chairman:	Chancellor of the Exchequer (or Prime Minister when appropriate)
Members:	Foreign and Commonwealth Secretary (or representative)
	Secretary of State for Trade and Industry
	Secretary of State for Transport
	Attorney General
	Financial Secretary, Treasury

5. Are you content that I should make arrangements on these lines?

Approved by
ROBERT ARMSTRONG
and signed in his absence.

21 December 1984

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COMMERCIAL

Treasury Chambers, Parliament Street, SW1P 3AG

GEOFFREY PATTIE ESQ MP
MINISTER OF STATE FOR INDUSTRY
AND INFORMATION TECHNOLOGY
Department of Trade and Industry
1-19 Victoria Street
London SW1H OET

21st December 1984

Dear Minister,

BRITISH AEROSPACE

Thank you for your letter of 21 December and enclosure from Lazards.

I agree with Lazard's assessment that a combined disposal and issue of new shares at the end of March should be ruled out. Quite apart from my doubts about the wisdom of BAe associating the disposal with a capital raising exercise, there are obvious risks in attempting an operation of this scale in close proximity to the Budget. For this reason I doubt whether it would be worth beginning preparatory work for a joint operation until we have decided on a course to follow.

In any event I think we should continue to press for our original idea, a disposal of the Government shareholding in mid-February. I do not believe that the company's proposal to combine this with an offer of new shares to the value of £150-£200m is in the best interests of the Government or of the company. It implies a total sale to the market of well above £500m at current market rates. With every respect to Kleinwort's judgement and the fact that I know Lazards too believe a sale of this order to be feasible, there must be risk that when the time comes the underwriters will claim the need for a very large discount to ensure a successful sale. In this event both parties lose out, and quite unnecessarily.

Our proposed approach, of a disposal of the Government holdings in February, with the company making a rights issue a year later offers a much better prospect of both the taxpayer and the company achieving a satisfactory outcome. I know that BAe and Kleinwort take the view that a two year gap is needed. But Lazards believe a 12 month gap would be sufficient, and I see no reason why this view should be dismissed.

I recognise that Sir Austin Pearce and his Board do not accept this assessment. I am convinced that we should re-open the discussion and attempt to persuade them to our point of view. We have, I believe, a strong case.

First, it must be helpful for the company to get the Government shareholding out of the way. Currently this holding overhangs the market and will continue to do so since our intentions to dispose of it are publicly known. Once this hurdle is over the company will be left with a clear run in 12 months time.

Second, I find it difficult to understand why the company should believe it crucial that the funds should be raised this year. I am advised by our accountants here that the BAe accounts for 1983, the first half year results in 1984 and the forward forecasts that were provided to us by the company when they made their application for launch aid for the A320, suggest that their financial position is in fact a strong one. There is no obvious need for them to raise working capital for a good many years.

I am afraid that I do not see your proposal that Lazards might purchase our shares under a no risk guarantee as a starter. As you describe the deal it would amount to no more than Lazards lending the Government £350m on short term account. I have no doubt that Lazards charges for this accommodation would be rather more than the cost of our borrowing similar money in the market. In addition we would be accepting an unquantifiable risk which could come home to roost in 1985-86. I rather suspect PAC might have something to say about a deal like that.

We are left, therefore, with our mid-February proposition. As you know this is important to us for general financing reasons. I think this must now be pressed on the company in an early meeting at Ministerial level. The opening position should be that Treasury Ministers have rejected the compromise which I understand has been mentioned to the Chairman and that we are not convinced that the company needs to raise new equity at the same time as the disposal of shares. (I hope that Lazards will take a critical look at the company's case, perhaps starting from the work our accounting advisers have done. A copy of their advice is attached for your officials) Only if this approach is put across strongly will the company be convinced it should move from its present negotiating position, which experience in these matters suggests is likely to be exaggerated.

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COMMERCIAL

However at the end of such a meeting I will be prepared to accept a compromise if it would secure BAe's agreement. I understand that if a company raises additional capital up to 10 per cent of the value of its issued share capital an abbreviated prospectus is all that is needed. This means that the same short and easily prepared prospectus which would cover our disposal would be sufficient for the new issue as well. On current valuation a 10 per cent issue of new funds would raise for the company some £75m. They might perhaps think that this is sufficient for them to strengthen their balance sheet at least for the next two years, although it is well below what the company currently have in mind. However, if they went for this option it would give them the not insubstantial prize of needing to issue only an abbreviated prospectus rather than to go through the time consuming and expensive procedure of a pathfinder and full prospectus. This course is not particularly attractive to us. It means that the selling operation in mid-February would still be on a big scale, and the price would be likely to be affected to some extent. There would not be much time for a selling campaign to help sustain the price. Both sides would need to consult Merchant Bank advisers, so that any proposal to Sir Austin Pearce should be made without commitment. But I suggest a Ministerial meeting should be set up urgently so that we can make the most of this approach. Official level meetings would also of course have to take a compatibly hard line.

I am sending copies of this letter to the Prime Mininster and to the Secretary of State for Defence.

yours sincerely

FPBrogan

for JOHN MOORE
(approved by the Financial Secretary and signed in his absence)

CONFIDENTIAL

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

Prime Minister

To note the latest position

David Peretz Esq
Private Secretary to
The Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
HM Treasury
Treasury Chambers
Parliament Street
LONDON SW1P 3AG

21st December 1984

Bad news

27/12.

Dear David,

BRITISH AIRWAYS: LAKER LIQUIDATOR'S SUIT

At the Prime Minister's meeting on 17 December my Secretary of State reported on the current state of the negotiations between British Airways and the Laker Liquidator for a settlement of his action against BA and other airlines in the US courts. The meeting felt that, if a settlement could be reached with the Liquidator on terms close to those my Secretary of State had indicated, it would be advantageous to settle. We have therefore encouraged British Airways to continue the negotiations.

British Airways and their legal advisers came to see officials here yesterday to bring us up to date with progress. Firm figures have not yet emerged. The estimate of around $80m for a settlement by all the airline defendants which my Secretary of State indicated at the Prime Minister's meeting still looks right; but there are two main areas of uncertainty:

(i) Although the figure of $80m includes an element for settlement with Sir Freddie Laker personally, this part is still particularly uncertain.

(ii) It is also unclear how much the European airline defendants will be willing to contribute; so far they have jointly offered $7.5m, which BA's negotiator has dismissed as inadequate. BA are hoping to talk this figure up somewhat, but we do not know how far they will succeed.

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BA's best estimate of their own contribution to the settlement has now gone up - largely because of the disappointing offer from the European airlines - to $35m to $45m. Pan Am and TWA might each contribute $8m-$10m. All the figures are, however, still very uncertain. BA hope to have a definite proposition for their Board and for Ministers by the end of the first week of January.

My Secretary of State doubts the defensibility of the settlement as it is now emerging, although the costs of a settlement must ultimately be weighed against the enormous potential liability and the risks of continuing the litigation. He sees great difficulty in explaining to Parliament and the public why BA should pay much more than the American airlines involved (BCal and the European airlines are in another category because the charges against them are different). He has asked BA and their negotiator to try to achieve an agreement whereby the shares of BA and Pan Am, if not also of TWA, are less unequal. We have encouraged BA to press ahead with the negotiations, without committing the Government; and we will report again as soon as we have clearer information from BA on the terms available.

BA's negotiator considers that continuation of the public uncertainty about the target date for privatisation strengthens his hand in pressurising the other parties to settle quickly, and to make their maximum contribution . It is therefore our intention if possible to make no statements to the Press over the Christmas and New Year period beyond the defensive line we have already agreed. We are, however, preparing, in consultation with other Departments concerned, a press announcement of a substantial deferment of privatisation, against the contingency that we are forced into making a formal statement.

I am sending copies of this letter to Andrew Turnbull (No 10), Len Appleyard (Foreign & Commonwealth Office), Henry Steel (Law Officers' Department), Callum McCarthy (Department of Trade & Industry) and Richard Hatfield (Cabinet Office).

Yours,

Diana

MISS D A NICHOLS
Private Secretary

THE WHITE HOUSE

WASHINGTON

December 21, 1984

Dear Margaret:

Thank you for your recent letter concerning civil aviation.

I remain hopeful that we will be able to improve the competitive conditions of international air transportation between our two countries. We are deeply disappointed, however, that you appear to condition new steps toward this goal on legislation that would eliminate private antitrust actions, especially since you and I share the goal of increasing competition in trade. I believe that more competition in air transportation between our two countries will serve both to benefit our consumers and to strengthen our airlines. This should not, in our view, be linked to a specific change in U.S. legislation which is at present unrealistic.

I have been informed that Secretary Shultz and Ambassador Price have explained to your ministers that we do not believe legislation to eliminate treble damages is necessary in order for our airlines to operate free of litigation in a more competitive environment. I further understand that adequate means are currently available under U.S. law, and our Bermuda II aviation agreement to provide any necessary protection from antitrust suits, as has been demonstrated by British Airways' long and favorable experience with U.S. antitrust law.

I am hopeful that after your ministers have reviewed the information Ambassador Price and others have provided them concerning U.S.

antitrust laws, you will conclude that we can open up the aviation regime without legislation on private antitrust suits. Indeed, we view such movement as essential if we are to be able in the future to contemplate any legislative action regarding private suits. I hope that you will be able to instruct your negotiators to resume our discussions promptly on this basis.

I look forward very much to seeing you Saturday at Camp David.

Sincerely,

Ron

The Right Honorable
Margaret Thatcher, M.P.,
Prime Minister
London

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Weekend Box.

Nicholson - thx
very helpful and

20 December 1984

PRIME MINISTER

AIRPORT INQUIRIES 1981-1983 - INSPECTOR'S REPORT

The task of coming to grips with Graham Eyre's 2,600 page report on the 1981-1983 Airports Inquiries is not as formidable as might initially appear. The challenging parts of the report, dealing with the need for a "coherent, logical and reasonable framework for the solving of the problems of meeting additional demand for airport capacity", are contained in 3 of the 9 volumes. The rest is the essential detail of any major planning inquiry.

Eyre has done a good job in marshalling the evidence of 250 witnesses and 4,000, often lengthy and complex documents, into a well-structured, accessible and readable form. Accepting the length of the report as inevitable, he has written it in a manner designed to assist those dipping selectively to obtain an appreciation of specific aspects.

You may have seen that Transport and Environment have compiled a volume of extracts from the Report. Whilst useful, this does not adequately capture the historical analysis which forms the basis of his contention that:

"The history and development of airports policy, on the part of administration after administration of whatever

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political colour has been characterised by ad hoc expediency, unacceptable and ill-judged procedures, ineptness, vacillation, uncertainty and ill-advised, precipitate judgements."

Nor does it properly convey the depth and quality of the analysis of future options which seeks to prepare the ground for the manifestly difficult decisions required to achieve a coherent airports policy.

The path we would signpost through the report is mapped out below. Before setting out you will need a definition of the most frequently used abbreviations. A basic list is appended.

1. VOLUME 1, PART I - INTRODUCTION

1.1 The one-page Preface provides a nice vignette of Graham Eyre and his style.

1.2 Eyre's comments on the public inquiry system (Section 3) are worth a quick scan.

1.3 The three-page Summary of Overall Conclusions at the end of Part I provides a very succinct preview of a long and complicated journey.

6.88 Quick · [illegible]

2. VOLUME 2, PART II - BACKGROUND, POLICIES, AIR TRAFFIC DEMAND AND CAPACITIES

2.1 Chapter 1 can be given a miss; it deals with the mechanics of the inquiries.

2.2 Chapter 2, charting the post-War history and development of airports policy, is extensive and well worth attention. It leaves one sympathising with the sentiments of an earlier venturer in the field of airports policy:

> "There is no more difficult area for public policy than airports. I am not so foolish as to believe that anyone can be satisfied with airport policy, except, of course, those whose areas have been reprieved. But the Government have a public duty and responsibility to look into the future and to take the harsh decisions which that future dictates."

One is struck by the changes of mood and outlook which no doubt reflected the prevailing spirit. Thus, as recently as 1953/4, when Gatwick was being contemplated, its role was seen as being limited largely to receiving aircraft diverted from Heathrow when visibility was poor. There were to be very few scheduled services and, in any case, the use of Gatwick would be restricted to short distance and charter operations.

By the mid-1960s, faced with the prospect of a major three-runway airport at Stansted, the Inspector who led the public inquiry reeled back, concerned at the environmental impact and the regional planning implications. Accordingly, he proposed a wide-ranging review of Stansted set in the context of a national airports policy in order to establish whether Stansted could be "justified by national necessity". In 1967 the Government responded with a White Paper which set out to refute the Inspector's findings and went on to propose an even more ambitious scheme for Stansted - "the third airport should ultimately be capable of development to the largest practicable capacity - namely, to that of two pairs of parallel runways".

Eyre's comments on the 1967 White Paper are damning:

- "It is the most extraordinary exercise I have ever seen in a document emanating from Government. Where the unknown authors seek to disagree with the Inspector, they seem conveniently to have forgotten that the witnesses called on behalf of the Ministry made major concessions under cross-examination and they largely ignored the evidence of other witnesses called by objectors, to which the Inspector obviously attached considerable weight."

- "It must appear to any fair-minded person who knows the facts, as grossly unfair to the Inspector. It

can only be described as a lamentable piece of decision-making. Its content is entirely unconvincing and it contains a number of errors. Government wholly failed to judge the climate of public opinion or to foresee the sense of outrage that the White Paper would provoke."

That outrage led to the Roskill Commission - a massive exercise in analysis and planning. Evidently, the presumption was that the right solution could be found simply by applying enough brain power of the requisite calibre. This was the tail-end of the period of unparallelled post-War growth. Concorde was on the drawing board. Roskill anticipated that by 1990 the London airports would need to handle 122 million passengers per annum - exactly double the planning estimate now proposed by Eyre. Consistent with the spirit of 1970, Roskill induced the Government to opt for another Concorde - Maplin Sands.

Maplin survived 39 months, foundering in the aftermath of the first oil crisis in 1973-4 and the growing awareness that the visions of unlimited economic growth, which characterised the late 1960s and early 1970s, were unrealistic. Unfortunately, the collapse of Maplin led to a scramble to undertake Heathrow Terminal 4 on an inferior site within the existing operational boundaries of the airport. With hindsight there would have been time to implement more favourable options, notably, the

E.R.

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removal of the Perry Oaks sludge works and the extension of the airport to the West.

The short introductory section of Chapter 2 is worth a quick glance. The lengthy Section 2 gives a blow-by-blow account of the history and development of airports policy. You could skim it, or instead rely on Eyre's extensive commentary in Section 6, since this incorporates much of the history as well as discussing the implications. En route to Section 6 it is worth noting Eyre's encapsulation of the elements of the national airports policy as it has evolved so far. This is set out in the two pages of Section 3. Sections 4 and 5, in which Eyre considers the relationship between the Stansted/T5 planning inquiries and national airports policy can be skipped.

Eyre's summary of his impressions following a review of the history and development of our national airports policy (Sections 6.88 - 6.109) is certainly worth attention.

2.3 Chapter 3 covering regional policy and planning in the South East is not essential reading. The one page of conclusions set out in Section 5 will probably suffice.

2.4 In Chapter 4, Eyre rightly devotes considerable attention to the long-term forecasting of demand for air transport. The post-War history of airports planning reminds us that

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E.R.

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the differences of opinion between expert forecasters at any given time are overshadowed by alarming changes of outlook over comparatively short periods. Since the first oil crisis in 1973-4, successive forecasts have been progressively revised downwards. (Is Eyre's near doubling of demand by 2,000 still too optimistic?)

The introduction in Section 1 of Chapter 4 provides a useful understanding of the way in which Eyre and his team have approached the problem of forecasting future air transport demand. This is supplemented by Eyre's illuminating description (Sections 5.10 and 5.11) of his concept of "demand planning values". He explains that he has consciously pitched his planning values on the high side, on the grounds that the lead times for airport planning and development are long and that whereas it is relatively easy to aim high and subsequently have to ease off the accelerator, it is usually much more difficult and disruptive to respond belatedly to unexpectedly high demand.

Sections 2 and 3 of Chapter 4, discussing the many sources of air transport forecasts for London and the regions, can be passed over as unnecessary detail.

Section 5.2, dealing with the possibility of the demand for air transport reaching saturation at some point, is clearly important. Eyre concludes that if saturation were to become a factor it would arise beyond the horizon

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E.B.

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of any forecasts relevant to today's pressing decisions on airport expansion.

2.5 Chapter 5, dealing with the forecasts of Air Transport Movements (ATMs), is significant primarily because it confronts the Government's undertaking to limit ATMs at Heathrow to a maximum of 275,000 pa.

The introduction in Section 1 is useful background. The commentary in Section 8 of Chapter 5 reveals some of the complexities and conflicts of policy which must be tackled. As Eyre says - "an ATM limit in annual terms is a largely artificial concept. I am far from satisfied that this factor was fully considered at the T4 Inquiry". ATM limits also conflict with the Government's aim to deregulate air transport - the trade-off between environmental protection and competition. Section 9 sets out Eyre's conclusions.

2.6 Anyone using Heathrow at peak times, like a Sunday evening, will identify with the comment:

Chapter 6 =

end 7.14.

"Heathrow is the foremost international airport in the world and it should be unthinkable that overcrowding is to be tolerated. Heathrow's reputation has suffered in the past and still suffers because of overcrowding at peak times. Future development must be aimed at avoiding these conditions."

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Chapter 6 sets out to define the future load on terminal capacity - a load which needs to be considered not on the basis of annual averages, but peak hourly rates. Again, the introduction in Section 1 is a useful lead-in. The body of Chapter 6 can be skipped in favour of Eyre's commentary in Section 7 and conclusions in Section 8.

2.7 Chapter 7 deals with the question of whether runway and aircraft handling facilities at London's airports will be sufficient to meet future levels of air transport demand. You will probably find it sufficient to glance at the summary in Section 8.13 and the conclusions in Section 9.

2.8 Chapter 8 addresses the fundamental question of whether our national airports policy should always seek to meet the demand for additional airport capacity in the right place, by the right means and at the right time. The conclusion is yes, but not willy-nilly and at any price. The commentary (Section 3) and the conclusions (Section 4) should be sufficient for your purpose.

3. VOLUME 2, PART III - THE OPTIONS

3.1 In this volume you can confine your attention to Chapter 10. Chapter 9 is procedural. Maplin revisited (Chapter 11), Yardley Chase (Chapter 12) and Severnside (Chapter 13) are explored, but all prove to be cul de sacs:

- "Maplin should stay well and truly buried."

- "(Yardley Chase) should cease to be a potential geographical location for additional airport capacity to serve future needs."

- "A major new airport at Severnside should be ruled out now once and for all."

3.2 That leaves you with the contentious question of whether the airport requirements of London and the South-East can and should be decoupled from those of the rest of the country. Eyre examines this long-standing issue from all angles and concludes that:

> "The provision of further capacity in the South East will not deleteriously affect the regions or their airports in any significant respect and there are no grounds that would justify an embargo on the provision of such capacity."

Parts of the introduction (Section 1) are worth a quick dip:

- the background information in sub-sections 1.6 - 1.9;

- the expenditure on regional airports (1.23);

- the capacity of regional airports (1.24 and 1.26).

Eyre's summary of the background material (1.27 - 1.34) is very helpful. His General Commentary on the Various Cases (Section 6) is essential reading. His conclusion is that:

- Successive Governments have been and continue "actively seeking to encourage the introduction of more services in the regions".

- "There is no sensible mechanism available or likely to become available which would forcibly divert demand to regional airports."

- "Whilst competition from continental airports with modern facilities will undoubtedly grow, the London airports system must be fostered if it is to maintain its role as the most important international hub of air traffic in the world. Any attempt unduly to splinter the system's very function and thereby weaken its ability to perform its role would militate against the national interest. It was significant that airline operations with a strong commitment to the future success of regional airports nevertheless advocated the importance of securing sufficient and additional airport capacity in the London airports system."

The conclusions of Chapter 10 are set out in Section 7.

4. VOLUME 7, PART VI, CHAPTERS 48 - 54

This is the last leg of the journey. In Part VI, "The Total Context and A Coherent Strategy", Eyre draws together the strands of his analysis of the development of airports policy and the elements of a coherent future policy.

It is tempting to jump straight to Chapter 54, which is the ultimate summary. However, I would suggest that the intermediate steps are worth some attention.

3.1 Chapter 48 discusses the "Narrowing of the Options". As you will see from the conclusions in Section 12, the focus of attention is the decision in the 1978 White Paper to restrict Heathrow to a four-terminal airport. Eyre concludes that this "had the widest and most critical implications, not only for the future of Heathrow airport, but also for any subsequent decision or strategy for the future of the London airports system as a whole, in the longer term". For this reason, he argues that "the imposition of a capacity ceiling at Heathrow requires close investigation in the context of a future strategy for the London airports system".

3.2 Chapter 49 deals with the potential for Heathrow Airport. The brief introduction in Section 1 is worth a quick glance. You can then jump to the summary in Section 9, a reminder of the Outstanding Constraints on the development of Heathrow in Section 10 and the overall

conclusions in Section 11. At the end of the summary, Eyre firmly nails his colours to one mast:

> "It is remarkable that, after so many years and so many errors, the opportunity still exists to transform Heathrow from a second class facility into a magnificient airport worthy of its unique international status and its role as the major transportation gateway to London and the UK. There is no doubt in my mind that such a colossal opportunity should be seized so that Heathrow's success in the future is assured. I confidently predict that any other course would jeopardise the national interest in one of the few fields in which the UK still leads the world."

3.3 In Chapter 50, Eyre turns his attention to the potential for Stansted airport. Again, the introduction in Section 1 is worth a quick perusal. Thereafter you can jump to the summary in Section 8 and the conclusions in Section 9. Eyre argues that "there are overwhelming reasons why a second runway and further associated airport facilities should not be constructed at Stansted". On the other hand, he concludes that there are no overriding objections to developing the capacity of Stansted airport to 15 million passengers pa, by the early 1990s, and ultimately 25 million passengers pa.

3.4 In Chapter 51, Eyre attempts to relate his interim conclusions to the total context of London airports policy. Here, he looks at the alternatives of further development at Heathrow (ie from 38 million passengers pa to 53 million passengers pa) versus the expansion of Stansted airport beyond a one-runway system having an maximum ultimate capacity of 25 million passengers pa. His conclusion is that "the modest territorial expansion at Heathrow, with its limited consequences and overwhelming advantages, confirms, beyond doubt my conviction that such a development should never occur at Stansted, whereas the development at Heathrow must take place in the national interest. In so far as the two matters represent alternatives, it is a one-horse race".

Section 4 (where the balance lies) and Section 5 (conclusions) are worth attention.

3.5 Chapter 52 deals with the foreseen capacity requirements of the London airports system. Given the long lead times for airport planning and development, Eyre's comments on the position beyond the year 2000 (Sections 5.16 - 5.17) are of more than academic interest. The conclusions in Section 6 are brief.

3.6 Chapter 53 represents the penultimate step in Eyre's formulation of a coherent strategy. You could go straight to the conclusions in Section 10, but that would be doing less than justice to a good deal of substantial

material on the nature of the challenge confronting the Government, and on the future role of London's airport system. Perhaps your best course is to skim quickly through the whole of Chapter 53.

3.7 Chapter 54 is the ultimate summary entitled "A Coherent Strategy for the Future and Implementation". The first three sections - the introduction, the summary of the main relevant factors and a summary of the strategy, are certainly essential reading.

Section 4, dealing with the implementation and procedures is probably less important at this stage and deserves no more than a quick skim.

I hope these signposts make Eyre's report less impenetrable.

JOHN WYBREW

D. R.

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APPENDIX

COMMON ABBREVIATIONS IN THE EYRE REPORT

ACAP	Advisory Committee on Airports Policy.
ATFWP	Air Traffic Forecasting Working Party.
DPV	Demand Planning Value (assessed levels of passenger demand for which it would be prudent to plan capacity).
HE	Hertfordshire and Essex County Councils.
NOERC	North of England Regional Consortium.
SGSEA	Study Group on South East Airports.
TWA	Thames Water Authority.

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CC TF
Brighton
Press

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

Murdo Maclean Esq
PS/Chief Whip
Whips Office
House of Commons
LONDON
SW1A 0AA

20 December 1984

Dear Murdo

CIVIL AVIATION BILL

We have spoken about the draft of today's statement on the Civil Aviation Bill that my Secretary of State sent round yesterday, under cover of a letter to the Leader of the House.

I now attach a copy of what I hope will be the final version, with the amendments we discussed:

- the deletion of the sentence "effectively, the Committee has voted not to carry out its remit."

- the addition of a paragraph (now the penultimate paragraph) referring to the Chairman's decision to reconvene the Committee on 12 February. This paragraph, and indeed the whole statement, has been cleared with the Clerk of the Committee; and we are in touch with him on the matter of the extent to which the Secretary of State can go in answering supplementary questions and remain in order.

I am sending a copy of this letter to Tim Flesher at No.10, David Morris in the Leader's Office and Neil Kinghan in Ian Gow's office. I am also sending a copy to the Clerk - Douglas Millar.

Yours sincerely

Henry Derwent

H C S DERWENT
Private Secretary

DRAFT STATEMENT ON THE CIVIL AVIATION BILL

With permission, Mr Speaker, I would like to make a short statement about the Civil Aviation Bill.

The House gave the Bill a Second Reading on 21 November, by a majority of 78, and committed it to Standing Committee F for consideration. However, on two separate occasions, Tuesday 11 December and Tuesday 18 December, the Committee has voted against the Sittings Motion.

The Bill is required whatever decisions are taken in relation to the Inspector's Report on Stansted/T5. The Government will need the powers in the Bill if at any time it is decided to impose a limit on ATMs at any BAA airport for environmental reasons: equally it will need the powers even if the environmental limit at Heathrow were not imposed, because both Heathrow and Gatwick are rapidly approaching the point when demand for runway space will exceed the physical capacity for extended periods of the day.

Proceeding with the Bill would not therefore have prejudiced the decision my h.f. the Minister for Housing and Construction and I will have to take on the Inspector's Report. Nevertheless the Government suggests that further consideration of the Bill be postponed until that decision has been taken.

I note the Chairman has reconvened the Committee for 12 February. I must make it clear to the House that it is very likely that no decision on Stansted/T5 will be possible by then. We will therefore in due course seek to arrange through the usual channels with the Chairman when the Committee shall meet again.

I hope that this procedure will be in accordance with the wishes of the House.

FINANCIAL SECRETARY TO THE TREASURY

Treasury Chambers,

Parliament Street, SW1P 3AG

With the Compliments of the

Private Secretary to the

Financial Secretary

This is the advice prepared by our accounting advisers, mentioned in the final para 7 page 2 of the Financial Secretary's letter of 21 Dec. to Mr Pattie on British Aerospace. I apologise for the original omission.

FPBogan 27/12

CONFIDENTIAL
commercial

MR A LOVELL

From: D J KING
20 December 1984

cc Mr G Grimstone

BAe

You asked me to consider BAe's cash requirement over the next two years.

2. I have reviewed the forecasts provided by BAe as part of their launch aid application on the A320. To these I have added the effect of launch aid which I understand was agreed at:-

1984	1985	1986	1987	
62	73	85	29	(£ millions)

3. Based on BAe's figures, adjusted for launch aid, their net borrowing at the end of 1985 is £63m, a gearing ratio (defined as debt divided by debt plus equity) of 5%. The peak gearing ratio (11%) occurs in 1985. Furthermore, the net debt position of £34m projected for December 1983 turned out to be a net cash position of £30m. The profit before tax of £56m for the 6 months to June 1984 seems to put them well on the way towards the 1984 profit target.

4. 11% is a very modest gearing ratio. A business such as BAe could comfortably support borrowings up to a gearing of 33% - a view supported by Rothschilds, the merchant bank advising on the ROFs where we have recently had similar discussions.

Conclusion

5. Given that Government is 'front ending' the A320 launch aid, there is absolutely no substance in BAe's contention that they must raise £200m within the next year or so. Their own projections simply do not support that view.

6. It seems that BAe are simply trying to get a free ride on HMG's publicity machine. In their position, I would probably try the same argument. But if BAe have a cash requirement, it is surely in the late 1980's when launch aid has run out and A320 revenues are not yet flowing.

... 7. I attach a schedule of profit and borrowing projections.

D J KING

BAe - PROFITS

	1983	1984	1985	1986	1987	1988	1989	1990
Profit before tax (including A320)	90	57	55	105	108	139	198	298
Launch aid agreed	-	62	73	85	29	-	-	-
Interest effect at 12%		4	12	23	33	38	43	48
Profit before tax	90	123	40	213	170	177	241	336

BAe - NET CASH POSITION

Net cash/(loans) pre launch aid	(34)	(150)	(264)	(322)	(414)	(475)	(449)	(351)
Launch aid (cumulative with interest at 12%)	-	66	151	259	321	359	402	450
Net cash/(loans)	(34)	(84)	(117)	(63)	(93)	(116)	(47)	99
Equity								
Shareholders funds before launch aid	745	771	792	860	927	1021	1169	1388
Launch aid	-	66	151	259	321	359	402	450
With launch aid	745	837	943	1119	1248	1380	1571	1838
Gearing (debt as a percentage of debt + equity)	4%	9%	11%	5%	7%	8%	3%	N/A

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6.17

RESTRICTED

cc Powell

DF Lee
21/12

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

19 December 1984

Andrew Turnbull Esq
10 Downing Street
LONDON SW1

Dear Andrew

BRITISH AIRWAYS PRIVATISATION AND US ANTI-TRUST SUITS

The attached Chancellor has seen Dinah Nichols' letter to you of 18 December covering a proposed line to take in answer to press questions as to whether British Airways privatisation is to be delayed. He thinks that paragraph 3 of that line to take should be used only if pressed and should be amended to read:-

> "The Government has no plans to indemnify British Airways after privatisation against an adverse judgement in these law suits, in respect of which British Airways have denied liability."

I am copying this letter to Dinah Nicholls (Transport), Peter Ricketts (FCO), Callum McCarthy (DTI), Richard Gardiner (Attorney General's office) and Sir Robert Armstrong.

Yours ever
David

D L C PERETZ
Principal Private Secretary

CC

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

The Rt Hon John Biffen MP
Leader of the House of Commons
House of Commons
LONDON
SW1A 0AA

19 December 1984

Dear John

N 2012

CIVIL AVIATION BILL

I am attaching a copy of the statement that I would propose to make tomorrow on the Civil Aviation Bill. It follows the line agreed at Legislation Committee this morning that we should postpone consideration of the Bill in Committee until after decisions on the Inspector's report on the airports inquiries had been announced; and that I should invite Michael Shersby, the Committee's Chairman, to consider deferring sittings until that time.

Subsequently, we have been advised by the House Authorities that it would probably not be in order for Mr Shersby now to defer sittings until April, the earliest conceivable date at which we might be ready to announce decisions on the Inspector's report. They advise that Mr Shersby could defer sittings only until mid-February. We would then have to either seek to pass a Sittings Motion in the Committee to defer consideration of the Bill until decisions have been taken on the Inspector's report; or move a motion on the floor of the House that the Committee should resume its consideration of the Bill at a later date. I will be discussing these options with Michael Shersby this evening, but I do not think that our discussion is likely to require any significant change in my statement to the House.

I am sending copies of this letter to the Prime Minister and Ian Gow as well as to other members of 'L'.

Yours ever

Nicholas

NICHOLAS RIDLEY

DRAFT STATEMENT BY SECRETARY OF STATE ON CIVIL AVIATION BILL

With permission, Mr Speaker, I would like to make a short statement about the Civil Aviation Bill.

The House gave the Bill a Second Reading on 21 November, by a majority of 78, and committed it to Standing Committee F for consideration. However, on two separate occasions, Tuesday 11 December and Tuesday 18 December, the Committee has voted against the Sittings Motion. Effectively, the Committee has voted not to carry out its remit.

The Bill is required whatever decisions are taken in relation to the Inspector's Report on Stansted/T5. The Government will need the powers in the Bill if at any time it is decided to impose a limit on ATMs at any BAA airport for environmental reasons: equally it will need the powers even if the environmental limit at Heathrow were not imposed, because both Heathrow and Gatwick are rapidly approaching the point when demand for runway space will exceed the physical capacity for extended periods of the day.

Proceeding with the Bill would not therefore have prejudiced the decision my h.f. the Minister for Housing and Construction and I will have to take on the Inspector's Report. Nevertheless the Government suggests that further consideration of the Bill be postponed until that decision has been taken.

I hope that this procedure will be in accordance with the wishes of the House.

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

Tim Flesher Esq
Private Secretary
10 Downing Street
LONDON SW1

19 December 1984

Dear Tim,

BA PRIVATISATION AND ANTI TRUST SUITS

Following further discussions with FCO officials I attach a slightly modified version of the Prime Minister's brief and the Bermuda 2 note which I circulated late yesterday. The paper on the future arrangements deal (Annex B) and the suggested press line are unchanged.

Mr Ridley is now content for the brief and accompanying papers to be transmitted to the Prime Minister.

I am copying this to Peter Ricketts (Foreign and Commonwealth Office), David Peretz (Treasury), Callum McCarthy (Trade and Industry), Richard Gardiner (Attorney General's Office) and Richard Hatfield and Peter Gregson, Cabinet Office.

Yours,

Dinah

MISS D A NICHOLS
Private Secretary

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DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

Andrew Turnbull Esq
Private Secretary
10 Downing Street
LONDON
SW1

18 December 1984

PM ans 19/12

Dear Andrew,

BA PRIVATISATION AND US ANTI-TRUST SUITS

As agreed at yesterday's meeting chaired by the Prime Minister I attach a brief for the Prime Minister's meeting with President Reagan, a note on the Bermuda 2 Agreement and a suggested press line.

It occurred to us that it might also be useful for the Private Secretary to have to hand a paper outlining the deal on future anti-trust arrangements which was being negotiated. I attach a note on this too.

Mr Ridley saw and was content with an earlier draft. I will be putting this version, which incorporates points suggested by FCO officials, to him overnight. But in view of your timescale I trust that other Ministers will also be able to see the brief overnight.

I am copying this to Peter Ricketts, Foreign and Commonwealth Office, David Peretz, Treasury, Callum McCarthy, Trade and Industry, Richard Gardiner, Attorney General's Office, and Richard Hatfield, Cabinet Office.

Yours,

Diana

MISS D A NICHOLS
Private Secretary

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LINE TO TAKE

I greatly appreciated your courageous decision on indictments. Setting aside the past prepares the way for agreement about the future.

I know that you have no power to stop private suits. But the private Laker law suits and class action are still a serious problem. Causing me a high political cost in delaying privatisation of British Airways: no flotation prospectus can be written while they are outstanding. [No evidence of breach of English law or of conspiracy to bring down Laker. All the fares charged were approved by Governments.]

For the future we must avoid these problems. We both want more competition in air services on a basis of fair trade. For this we must agree the competition rules: in an air services agreement we both have to agree. Until we do, we may even be driven to regulate more, not less to protect ourselves against anti trust.

But it will not be enough for our Governments to agree the rules if you unilaterally apply court-based private enforcement (the treble damage suit): which has become a weapon of commercial blackmail rather than pro-competitive. Nor can we accept that the decisions of our authorities should be questioned in your courts. I was encouraged when your people offered last October (in a package including Government enforcement of agreed competition rules and for tariff liberalisation) to ask Congress for legislation to remove the private treble damage suit from our air services. Subsequent discussion made good progress.

So I was disappointed when following your decision your people seemed less keen and said they couldn't even discuss approaching the Congress for this legislation. I hope this hesitation by your people can be overcome.

To help the public atmosphere we have agreed to winter low fares (with assurances about Department of Justice enforcement but still taking some risk of private suits). We are also ready to start discussions on next summer's capacity.

Now we must set our negotiators to define the package of competition rules and liberalisation which can be available as soon as your legislation is passed. We can discuss timing when the package is defined. Hope you can put your full authority behind an early approach to Congress so that we don't have these problems again.

Objectives

That the President should be reassured that his decision was appreciated but made to understand that this issue is highly political for us as well. That he should recognise that in international air services both sides have to agree the rules including, fundamentally, the competition rules. That no resolution of the dispute is possible without the removal for the future of the private treble damage action; and that the Department of Justice offered this and then drew it back. That negotiations should be resumed at the point they had reached before his decision.

Background

US officials won't be willing to develop their view about Congressional problems before Congress returns in late January/ February - even then their views about early action may prove to be gloomy.

No US Administration can surely deliver the Congress (cf the Kennedy Round): so our strategy has been that the liberalisation package has to be prenegotiated and contingent on removal of the treble damage suit. Moreover, because the US airlines have a built in unfair trading advantage in their protected internal (cabotage) market and the Bermuda 2 agreement is already operated liberally, we do not have much more to offer in liberalisation anyway (beyond what has been put on the table) without producing unfair trading conditions for our airlines. What little there is, is needed for the final haul.

Annex A describes the Bermuda 2 Agreement. Annex B outlines the deal under discussion before the President's decision.

Annex A

THE "BERMUDA 2" BILATERAL AIR SERVICES AGREEMENT

Commercial air services can only operate (under international law) by agreement of the Governments of the countries served. This 1977 Agreement establishes the basis for UK/US Air Services. For scheduled air services it regulates:

(a) Market entry (by specifying agreed routes between UK and US "gateway" points and limiting the number of airlines of each side which may operate those routes).

(b) where necessary capacity on routes (the numbers of flights on routes).

((a) and (b) were and are necessary to maintain fair competition and avoid dumping. This is important to the UK, to prevent swamping by US airlines from their enormous and protected domestic network).

(c) Price (airlines propose fares. Either Government can, within agreed criteria, veto a fare. All fares require approval before they may be charged. This is called a "double approval" system.)

2 Other provisions of the Agreement deal with eg fair and equal competition, charter services, cargo services and the arrangements for services between the US and UK Overseas Territories.

3 The Agreement has been operated liberally; the North Atlantic is the most competitive international aviation market, US market share is currently of the order of 65%.

ANTI TRUST

4 Our view is that US anti trust law is not applicable to Bermuda 2 activities both on general and specific grounds. Generally, we say Bermuda 2 establishes a self-contained system which is regulated by aeronautical authorities in terms of market entry, supply, price and competition, and that aeronautical

authorities are required to police and safeguard the public and airline interests. Specifically we say that the tariffs Article 12 clearly envisages inter-airline tariff discussions and agreements and that enforcement of these provisions is the function of aeronautical authorities and aviation law, not of US domestic anti trust law.

5 The US argue that the UK sought specific exclusion of US anti trust in 1977 and did not get it, and that application of US anti trust law is consistent with Bermuda 2.

6 We believe that neither side got exactly what it wanted in 1977 and that in the circumstances of the time (when in practice no difficulties had arisen because there had been hardly any aviation anti trust cases and none against British airlines) both sides accepted a "stand off" on this subject, or in other words a "fudge".

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DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

cc Press Office

Andrew Turnbull Esq
Private Secretary
10 Downing Street
LONDON SW1A OAA

18 December 1984

Dear Andrew,

BRITISH AIRWAYS PRIVATISATION AND US ANTI-TRUST SUITS

Following yesterday's meeting of Ministers under the Prime Minister's chairmanship we were asked to put round a suggested line to take with the press in response to enquiries about a possible delay to BA's privatisation.

I attach a suggested line. I think it would be best if, so far as possible, enquirers on this subject are referred to this Department. If other Ministers or press officers need to say something themselves, Mr Ridley would be grateful if (subject to any comments from copy addressees within the next 24 hours) they would make use of the attached note unattributably, sticking as closely as possible to its exact words. It is important that we should not depart from this line - in particular that we should not imply that the delay in the privatisation timetable will be lengthy - if we are to give the current negotiations for a settlement of the Laker Liquidator's action the best chance of success.

My Secretary of State spoke to the Chancellor of the Exchequer after the meeting. They agreed that, though the possibility should be explored of providing an indemnity against anti-trust liabilities by transferring them to the British Airways Board (which still exists as a shell), that should not be revealed publicly, or to British Airways, because it could well affect the negotiations on a settlement. As the question of an indemnity has already been mentioned in the press, and Ministers may be asked about it, my Secretary of State considers that it will be necessary to take the line in paragraph 3 of the enclosure, unless and until Ministers decide to pursue such a course.

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I am copying this letter and the attachment to Peter Ricketts (Foreign & Commonwealth Office), David Peretz (Treasury), Callum McCarthy (Trade & Industry), Richard Gardiner (Attorney General's Office) and Sir Robert Armstrong.

Yours,

Dinah

MISS D A NICHOLS
Private Secretary

PROPOSED LINE TO TAKE IN ANSWER TO PRESS QUESTIONS

AS TO WHETHER BRITISH AIRWAYS' PRIVATISATION IS TO BE DELAYED

(NON ATTRIBUTABLE)

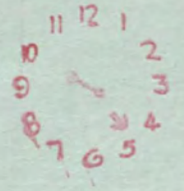
1. Yes, there is some slippage in the plans for privatisation of British Airways because of the uncertainties created by the application of US anti-trust law to air services under the Bermuda 2 aviation agreement, including the US civil law suits following the collapse of Laker Airways.

2. The Government remains committed to the privatisation of British Airways at the earliest possible date in 1985.

3. The Government does not plan to indemnify British Airways after privatisation against an adverse judgement in these law suits, in respect of which British Airways have denied liability.

4. /If appropriate/ The Government has never announced, or regarded, February as a firm date for privatisation. Our advisers have worked to a timetable culminating in mid-February as a planning date to enable us to be ready during the early part of 1985; but we have always recognised that the actual date could only be decided shortly beforehand, in the light of circumstances at the time.

Department of Transport
17 December 1984



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PRIME MINISTER

NEGOTIATIONS ON FUTURE ANTI TRUST ARRANGEMENTS WITH THE US GOVERNMENT

1. It is somewhat difficult to understand why, following President Reagan's very helpful decision on the enforcement of criminal anti-trust, the US negotiators last week sought to draw back in the negotiations on future arrangements, from their earlier proposal to remove the civil anti-trust treble damage suit from the services covered by Bermuda 2. How far this was due to an objective reappraisal of the difficulty of securing Congressional approval for the necessary legislation and how far to difficulties with the Department of Justice (DOJ) (who are sore at the President's decision) is not absolutely clear; Mr Dam's stance seems to reflect some hardening of attitudes of senior members of the US Administration, but it also contains some fundamental miscalculation about our position. But I am sure that it was right for us to resist any suggestion that it might be possible to negotiate a package without the all important provision relating to the removal of civil and anti-trust liability.

2. It remains to be seen whether the US will now use the 'pause for reflection', which was the best outcome to last week's exchange we could achieve given the tightness of the US negotiators' brief, to reassess their position and tactics. If not we may have to consider a combination of carrot and stick to get them back to the negotiating table. The removal of civil anti-trust liability for the future remains a cardinal objective for us; not only are private treble damage suits inappropriate, unpredictable and potentially very expensive, but the fact that US anti-trust law contains this independent court-based form of enforcement also severely limits the ability of the two governments to discuss and agree from time to time what should be the appropriate competition rules in our bilateral aviation relations.

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3. To encourage the US to adopt a more forthcoming attitude I think it would be appropriate to clear the remaining obstacles and approve low fares for this winter. This should be seen by the public in both countries as a positive response to the President's decision and might strengthen the more sensible voices in the Administration who wish to see the dispute resolved. However, if they do not show early signs of being ready to return to the negotiating table, I think we may also need to point out that if they insist on retaining civil anti-trust liability our air services agreement may need to regulate aviation much more tightly in order to limit the scope for the mischief of civil anti trust suits (and also - in that event why not? - to even up our market shares). I indicated to Ambassador Price when he called to see me today that this might have to be the alternative. I took the opportunity to restate our position on anti-trust set out in paragraph 2 above.

4. At this stage I hope that wiser counsels will prevail and that a reply from you in response to the President's recent message will encourage this. I should like the views of Sir Oliver Wright and of colleagues on a draft before submitting it to you.

a draft is being worked on.

5. On timing I am advised that, though it would be helpful, it is not essential for the BA prospectus to be able to record agreement on satisfactory arrangements on anti-trust for the future. I conclude therefore that we can afford, for a short while at least, to await developments on the US side. However, I would not wish to see the momentum lost completely and will be looking to get the Americans back to the table and in a reasonable frame of mind as soon as possible.

6. Copies of this minute go to Geoffrey Howe, Nigel Lawson, Norman Tebbit, Michael Havers and to Sir Robert Armstrong.

Denis Nicholas

pp NICHOLAS RIDLEY
4 December 1984

(approved by the Secretary of State & signed in his absence)

CONFIDENTIAL

2F

EL3ABK

bc John Wybrew (Policy)

10 DOWNING STREET

a MASTERSOT 17 December 1984

From the Private Secretary

BA Privatisation and US Anti-Trust Suits

The Prime Minister held a meeting today to discuss BA privatisation and US anti-trust suits. Present were the Chancellor of the Exchequer, Secretary of State for Transport, Attorney-General, Minister of State for Foreign and Commonwealth Affairs, Financial Secretary to the Treasury and Mr Fletcher. Also present were Mr Gregson and Mr Redwood.

The Secretary of State for Transport said that following President Reagan's decision not to proceed with the Department of Justice's criminal action against BA, three areas of litigation remained - the Laker liquidator's suit, the anti-trust class actions, and possibly future anti-trust cases relating to BA actions between 1977 and 1982. Progress had been made in negotiations with the Laker liquidator and it now looked possible to settle in the region of $80 million for all the airlines, of which BA's share would be $15-20 million. While the terms of a settlement might be known before Christmas an agreement could not be signed until later in January. This would make it impossible to proceed with the February date for the disposal of BA - indeed a delay of at least three months was likely. BA's total exposure under the class actions could be substantially greater and no prospectus could be signed until such actions were either settled or an indemnity was provided. This could occasion an even greater delay.

In discussion it was argued that privatisation of BA could be frustrated for the rest of the Parliament if no way could be found of divorcing present and future legal actions from the sale of BA. Furthermore, the knowledge that Government had a deadline for the privatisation of BA created an advantage for those bringing legal action. Work was needed to identify the options for separating BA plc from the residual liabilities arising from the legal cases. This residuary body would remain the responsibility of HMG. Any such solutions were likely to require legislation.

It was agreed that this course came close to providing an indemnity but it was argued that HMG was effectively at risk already - no new contingent liability would be acquired. Divorcing the legal cases from privatisation

would allow HMG a freer hand in deciding whether to fight the legal actions over an extended period or whether to settle out of court.

Summing up this part of the discussion, the Prime Minister said that if a settlement could be reached with the Laker liquidator on terms close to those indicated, it would be advantageous to settle. A decision on this should be deferred until the final terms were known. The Secretary of State for Transport, in conjunction with the Financial Secretary, should prepare a paper, for discussion with the Ministers concerned early in the New Year, on the options for divorcing the legal cases from privatisation. Meanwhile, if questioned on the timetable for the disposal of BA, Ministers could confirm that it would take somewhat longer than hoped to resolve the legal difficulties and that there would, in consequence, be some delay to the BA privatisation.

The discussion then turned to the negotiations with the US Government on air traffic across the Atlantic. Lady Young said the President had taken a courageous decision in calling off the Department of Justice's criminal case against BA. The Americans were disappointed with the UK's response to this step. It would be helpful if the UK could, at an early date, offer further steps towards liberalisation beyond the agreement already reached on winter fares.

The Secretary of State for Transport said the Government's objective had always been an agreement combining liberalisation with the removal of North Atlantic air traffic from the scope of US anti-trust legislation. While the President's action on the DoJ case was helpful, its benefit to the UK had been reduced by the news that the US administration now felt unable to offer any improvement in the position on anti-trust action. It was possible that the President had not fully appreciated the disappointment which this change of tack had caused to the UK.

Summing up this part of the discussion, the Prime Minister said she should continue to urge on the President that our objective was an agreement on liberalisation plus the removal of air traffic from the scope of anti-trust action. In view of HMG, it was wrong that fares agreed by the CAA and CAB should run foul of anti-trust legislation. While she should not offer any specific concessions, she could hint that further concessions on liberalisation could be offered if progress was made in negotiations.

She asked for a brief to be prepared which should reach her before her departure from Hong Kong. This should provide the line she should take with President Reagan; the line she should take at any press conferences; and a short note on the working of the Bermuda 2 Agreement. In order to meet the Prime Minister's deadline, a draft of the brief should be circulated to Treasury, Foreign Office and Cabinet Office by close on Tuesday, so that it can be completed by Wednesday, to reach desks in Hong Kong during the afternoon of Thursday.

I am copying this letter to Len Appleyard (Foreign and Commonwealth Office), David Peretz (HM Treasury), Henry Steel (Law Officers' Department), Callum McCarthy (Department of Trade and Industry) and Richard Hatfield (Cabinet Office).

(Andrew Turnbull)

Miss Dinah Nichols
Department of Transport

CONFIDENTIAL

NBPM AT 17/12

PM are providing a guide through the report which will supersede this

PRIME MINISTER

14 December 1984

AIRPORTS POLICY

Graham Eyre has thrown down the gauntlet for this Government to break out of the muddling-through mould and take a cool, strategic look at airports policy in the wider context of a coherent aviation policy. His challenge derives both from the breadth of the remit he has assumed and the quality of his analysis and report.

You will be widely applauded for undertaking to read Eyre's magnum opus. Firstly, his report deserves it. Secondly, you have signalled to the passionate special interest groups that a matter of considerable national importance should be approached carefully and with an open mind. Politically, the parcel he has passed us is fraught with problems.

One lobby can safely be appeased. Graham Eyre fully supports the expansion of traffic through the regional airports. The proposed expansion of terminal capacity at Stansted is seen as having little or no influence on the growth of passenger movements through regional airports from 22 million per year to 43 million per year by 2000. Moreover, given tough restrictions on night movements to and from the London airports - the likely price for continued expansion - more of the charter business is likely to migrate away from London. This is a high growth sector of the market.

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Efficient operators like Brittania can only offer cheap travel to holidaymakers by keeping their aircraft in the air 17-19 hours per day over the peak Summer period. This mode of operations inevitably requires some night movements.

More charter business for the regional airports should promote a virtuous circle, with improving airport facilities in turn attracting more scheduled international flights. Quantas, for example, have now hit the ceiling at Heathrow and moved 2 Australian flights per week to Manchester. Singapore Airlines are not far from the same point. We should advertise the fact that an airport like Manchester is open for more business and would welcome it, point out what we are doing to improve access to Manchester; and explain that any airlines wishing to run services would get a welcome.

We are left with the politically-difficult question of how to handle a near doubling of traffic (47 million passengers per year to 89 million) in the South-East between now and 2000. It is tempting to point to the progressive scaling down of past forecasts - particularly in the aftermath of the two oil shocks - and suggest that today's projection may well be over-optimistic.

Unfortunately, the problem has wider and more complex dimensions such as the seasonal and peak hourly demands on airport capacity. It is also significant that Eyre's recommendation of a Terminal 5 at Heathrow, pushing annual capacity from 38 to 53 million passengers, implies an increase

in the average number of passengers per flight from about 100 to 180. That probably flies in the face of Nicholas Ridley's efforts to liberalise air travel by stimulating genuine commercial competition - often in small, efficient aircraft capable of rapid turn-around.

One is also tempted to consider the scope for making greater use of Luton. Moreover, Birmingham is within reach of many travellers who would otherwise regard Heathrow as their only outlet. Both offer some scope, and this should be used, but they are likely to be limited by safety and air traffic control problems.

Conclusion

Graham Eyre has laid down a commendable, but politically difficult, challenge. He deserves to be read and carefully considered before options are closed.

Nicholas Ridley will hit this problem in the Commons Committee on the Civil Aviation Bill, to erect controls for air transport movements. We understand that the line he will take is:

- to concede the need to consider Eyre's report carefully before reaching a final decision on the 275,000 ATM limit at Heathrow;

- to maintain that irrespective of that decision controls will be required in due course - hence the need to preserve the Bill.

It will probably be inferred that he is still pro-Stansted. It may be better to put the Bill on ice until the Government has formulated a coherent airports policy.

JOHN WYBREW

E.R.

CONFIDENTIAL

MR TURNBULL

14 December 1984

BA PRIVATISATION

BA are now talking about a settlement with the Laker liquidator costing $50-70 million for all the airlines. BA's lawyers have also revised downwards the likely damage from class actions to a middle case of $85 million. Dunlop, of BA, also thinks some of these are insurable.

Treasury are sceptical about this optimism but may be prepared to contemplate either short legislation to transfer the liabilities under the law suits to HMG or offer a guarantee.

We should not give up hope and we should keep up the pressure to privatise.

JOHN REDWOOD

CONFIDENTIAL

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PRIME MINISTER

BRITISH AIRWAYS PRIVATISATION AND LAKER

I am circulating this note on further developments since my minute of 10 December and commenting on some of the points in the Foreign Secretary's minute of 12 December.

Quite a bit of progress has been made on our exploration of a global settlement of the liquidator's action. Both the creditors and the other airlines (European and American) are being realistic. The major outstanding question is how much Sir Freddie Laker will demand. The position is unlikely to be finally clear until later next week. As for figures, the working assumption on which discussions are taking place with the airline contributors is that the creditors would need $60 million (provided that certain major creditors in fact agree to reduce their claims). In addition to this there are as yet unquantified claims by Sir Freddie Laker and his US attorney. So it is not certain what people will in the end settle for. It looks as if British Airways' share may be much less than the £75 million figure mentioned in my earlier minute. A settlement of this action would have the advantage of limiting the real risk of further actions arising from the continuation of the US discovery processes in relation to it; and also of the problems which would arise if it is fought further and the US Judge chooses to combat the continuation of our blocking Order and Directions under the Protection of Trading Interests Act by making adverse findings of fact against British Airways.

But a settlement of the liquidator's case still leaves serious problems in relation to privatisation. British Airways' present US legal advice is that it would not be possible to settle the class action earlier than a year from now; and that until it is settled other steps to reduce their exposure to further private suits are not feasible. The figures we have been quoted for their possible exposure go up to $240 million for the present class action. There is in addition a third province of possible class actions beyond that. A very crude estimate of the potential

maximum liability if BA lost a case about collusive price-fixing with TWA and Pan Am between 1977 and 1982 amounts to a further $600 million. There is grave doubt as to whether the risks are insurable; and British Airways consider that they cannot in any case evaluate that until the liquidator's suit has been settled. But under the threat of these class actions, there is no question of BA's Board being able to sign a prospectus.

I must emphasise that all these figures depend crucially on the fairly arbitrary assumptions which one makes. I have been taken by British Airways' US counsel through the sort of calculations which are involved. The experience has fully borne in on me the horrors of the US treble damage anti trust action (combined with the contingency fee system, the US discovery processes and the fact that a successful defendant can recover no costs) which have turned this from an instrument for justice into a weapon for commercial blackmail. In any case, as the Foreign Secretary knows, 95% of these cases are settled and in a settlement the cost all depends on what the other man will accept. It is all too true that Lord King's judgement about the importance of the cases for privatisation has fundamentally changed since his remark to the American Ambassador: I commented on the behaviour of the BA board in my earlier minute. As for George Shultz' argument, there is a fundamental difference between the continuation in the New York stock market of a quotation for a company faced with anti trust litigation, or perhaps even a modest rights issue there, and the problem of selling in its entirety a company bigger than any previous flotation (British Telecom apart) on the London Stock Exchange. But the fundamental point is that BA's potential exposure is such that our rigorous disclosure requirement prevents our proceeding.

I am clear that without the resolution of all the private actions, privatisation cannot be achieved for at least a year unless the Government gives BA a general indemnity against all anti trust liabilities which they may have incurred to the present. I set out in my previous minute the powerful objections to such an

indemnity which have led us all to recommend against it. If the liquidator's action can be settled quickly at a sum we can accept I believe that it will be the best course. But I do not think we should yet exclude the possibility that BA should fight the class actions hard with the aim of securing an early resolution (or possibly settlement.)

As for the negotiations with the US over future arrangements, I think we must await the President's reaction to your message. The situation we are in now is intolerable. Privatisation is effectively prevented because of US Court actions, for things allegedly done by our airlines which were legal under our own law. This is a major political setback. In addition, we will have to make an expensive settlement out of Court. This will be followed by having to fight, or settle, at possibly even greater expense, the class actions.

If in addition to this we make an agreement with the Americans which does not for the future get rid of the civil treble damage suit and which contains liberalisation measures on the North Atlantic which can only be of benefit to US airlines at our expense, we have in sum an absolutely impossible political passage. It would be impossible to sell such a craven series of capitulations to our backbenchers and public opinion.

I have told the American Ambassador that I am ready for negotiations to continue on the whole package previously discussed without pre-conditions about the timing of US legislation (for which we have never asked). My impression is that, unless the President decides otherwise, the US position will not be re-evaluated until the return of the Congress at the end of January/early February permits soundings of Congressional leaders. We can make some gestures of goodwill now. We can agree in principle on low winter fares; we can start talks on next summer's capacity when our preparations are complete (though there are difficult issues for BCal here). I do not think we should go

further. It would be fatal to give unilaterally virtually all the US commercial interests want with nothing in return. In particular we are certainly not substantially operating a double disapproval system at present: if we had been we could not have stopped the low winter fares, which is what started the earlier movement on the US side.

In addition, the public presentation of all this raises very difficult issues.

I am sending copies to the Foreign Secretary, the Chancellor of the Exchequer, the Secretary of State for Trade and Industry, the Attorney General and to Sir Robert Armstrong.

Yours

pp NICHOLAS RIDLEY
14 December 1984

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

10 DOWNING STREET

Prime Minister

Since the meeting was postponed on Thursday the Foreign Secretary has minuted (Flag C) urging a forthcoming approach in negotiations with the US. The Transport Secretary has minuted (Flag D) arguing that legal position is extremely difficult and that we should concede as little as possible now.

AT 14/12

MJ

CONFIDENTIAL

CC NO.

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

CDP
1. SP to note
2 NB PM AT 13/12

The Rt Hon Michael Heseltine MP
Secretary of State for Defence
Ministry of Defence
Main Building
Whitehall
LONDON
SW1

13 December 1984

Dear Michael

FALKLAND ISLANDS TROOPING CONTRACT FOR BRITISH AIRWAYS

When I was trying to persuade British Airways and British Caledonian to agree to a number of route swaps last summer, in response to the recommendations of the Civil Aviation Authority's review of competition in air transport, you kindly agreed to award BA a contract to provide trooping flights to the Falklands, for which they had tendered at your Department's invitation. That was a most helpful gesture which enabled BA to relinquish their claim to take over BCal's Atlanta service as part of the route exchange. That had proved a sticking point for both airlines which threatened to make it impossible to agree on any swaps at all.

The negotiation of a contract with British Airways was of course a matter for your Department, but my officials have kept in touch with yours, and this has enabled us to deal with a tricky problem which emerged. Part of the arrangement which you and I agreed, was that BA would be able to lease back two Tristar aircraft from the RAF. We understood that they were needed to carry out the Falklands contract, but it subsequently transpired that BA wanted them for quite different commercial services, and proposed to lease a 747 aircraft for the Falklands flights, which they regard as more economic.

I recognise that it was unreasonable of BA to expect to use RAF aircraft in the long term for purely commercial services, and with some difficulty I have succeeded in persuading British Airways to look elsewhere for those aircraft. They have reluctantly done so, and made other arrangements, albeit at a price higher than was contemplated in our discussion. They were also looking for a contract for at least 3 years, but are now I understand prepared to accept an MOD commitment of a minimum of 1 year.

So British Airways have reduced very considerably what they were asking for when I raised the matter with you. I was therefore very disappointed to learn from my officials this week that MOD had now told British Airways they could no longer

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contemplate a contract of the kind for which they originally invited tenders, but were only interested in a joint operation using RAF Tristars on the route with a modest level of engineering and possibly other support for them by British Airways, similar to that which has been given since you bought Tristars from them 2 years ago.

British Airways have complained to me very angrily that the Government are trying to wriggle out of a commitment which they gave in order to secure BA's co-operation over the competition review, and I feel, particularly since what they thought they were getting has already been pared down, that they have every right to be aggrieved.

There is no doubt in my mind that what we agreed to give them was a straightforward charter contract: it is true that we were wrongly under the impression that it would be carried out with leased RAF Tristars, but the airline had already tendered on the basis of 747s, and I understand that operationally 747s would be more welcome at the new Falklands airport. The concept of joint operation with the RAF has emerged since our agreement was reached. But I do not think that we can go back on what we agreed, and told British Airways, because the RAF now see a more economical way of meeting their requirements. After you had agreed to place a contract with BA, and following the initial discussions with your officials, the airline entered into a commitment to lease a Boeing 747 which would be used primarily on the Falklands route, and in its spare time would serve other BA commercial routes. That is now integrated into their operational plans for next summer. If they are not to have the Falklands contract, they will not necessarily be able to find other ways of occupying it on those 4 days.

I understand your officials will be reporting to you where matters stand, and I must urge you to adhere to the clear commitment which you gave me in September. The prospect of the contract was given some publicity, and if British Airways end up with nothing out of it at all, I fear they may themselves withdraw from the commitments about the route swaps. Since those formed the major element of the Government's response to the Civil Aviation Authority's review, and were in fact a good deal less extensive, and less favourable to the independent airlines, than CAA had proposed, such action by British Airways would put the Government in a very embarrassing position.

I am copying this letter to the Prime Minister and to Nigel Lawson, Norman Tebbit, John Biffen and Sir Robert Armstrong.

NICHOLAS RIDLEY

CONFIDENTIAL

~~Leak~~
CAB

Foreign and Commonwealth Office

London SW1A 2AH

13 December 1984

Dear Charles,

British Airways Privatisation and Laker

We have spotted that, as a result of a typing error, a phrase appeared in the Foreign Secretary's minute to the Prime Minister of 12 December on the above subject which should not have been there. Could recipients please delete the following phrase in brackets in the last sentence of paragraph 3:

(copy att).

"in practice the CAA are already substantially operating a 'double disapproval' regime".

I am copying this minute to the Private Secretaries to the Chancellor of the Exchequer, Secretary of State for Transport, Secretary of State for Trade and Industry and the Attorney General.

Yours ever,

Peter Ricketts

(P F Ricketts)
Private Secretary

C D Powell Esq
10 Downing Street

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Ref. A084/3337

PRIME MINISTER

Cabinet: Parliamentary Affairs: Civil Aviation Bill

BACKGROUND

The Civil Aviation Bill is mainly designed to implement a Government commitment when giving planning approval for Terminal 4 at Heathrow Airport for an air traffic movement (ATM) limit of 275,000. This limit is to come into effect when the terminal opens next autumn. The Bill does not itself contain the limit; it enables the Secretary of State for Transport to give directions to the British Airports Authority in respect of the number of movements which may be permitted at any airport.

2. The Bill was due to be taken in Committee in the House of Commons for the first time on Tuesday 11 December. In the event, the Government were unable to secure the sittings motion. The main argument mounted by its opponents (which on this occasion included three Conservative MPs) was that there had been insufficient time for them to consider the implications of the Inspector's Report on Stansted and Terminal 5 at Heathrow. This Report is currently with the Secretaries of State for Transport and for the Environment for decisions on a number of planning applications in connection with the expansion of Stansted and the construction of a fifth terminal at Heathrow. It recommends an increase in the number of passengers to be handled at both airports (a further 14½ million at Stansted in the short term and a further 15 million at Heathrow in the mid-1990s). The recommendation conflicts with the Government's commitment to an ATM limit of 275,000 at Heathrow.

3. The Lord Privy Seal will explain that the defeat in Committee seems unlikely to be repeated, because one Conservative Member is prepared to support the Government in securing a future sittings motion. However, difficulties can be expected in continued discussion of the Bill. Nevertheless, the Secretary of State for Transport has decided that the best course of action is to continue and to explain to the House that the enabling powers contained in the Bill do not prevent him from exercising his quasi-judicial functions in respect of the Inspector's Report.

HANDLING

4. The Lord Privy Seal will introduce the item and you may wish to ask the Secretary of State for Transport for his views. The Lord President may wish to comment in the context of the general presentation of Government policy, as well as possible handling problems in the House of Lords.

5. Other Cabinet members with an interest in the Civil Aviation Bill are the Secretary of State for the Environment (who has disqualified himself from taking decisions on the Stansted Inquiry) and the Secretary of State for Scotland (the Civil Aviation Bill also deals with the preconditions for the disposal of certain Scottish aerodromes).

CONCLUSION

6. Unless there is strong opposition in the Cabinet to the proposal that the Government should continue with the Civil Aviation Bill, you will merely wish the Cabinet to take note of what is being proposed.

RCA

12 December 1984

ROBERT ARMSTRONG

BRIAAA

PM/84/190

PRIME MINISTER

British Airways Privatisation and Laker

1. I have been thinking further about this since you sent your message to the President, and since we had a word about my short discussion with George Shultz. I think that the passage ahead will require careful political management and that we need to give firm guidance to our officials. The most immediate deadline is of course your meeting with President Reagan on 22 December. But I am also very conscious of the conflicting problems we face over privatisation itself.

2. It was clear to me from my exchange with George Shultz that the Americans do not feel that our response so far to the President's decision is politically adequate, and that in any case for the time being they cannot go to Congress to seek legislation on treble damages to put our aviation relationship on a mutually-agreeable legal basis. George Shultz naturally welcomed the news that we were working rapidly to introduce low winter fares. But something else is clearly needed before you see the President.

3. I believe that it is in our long-term interest to help the President meet his immediate political requirements. I know that Department of Transport officials are working hard on a further offer to the Americans which they might accept as a step towards "liberalisation". But I understand that the work is going slowly because of the technical and commercial complexities. These have to be fully considered; we should not simply hand over to the Americans commercial advantages they have been seeking for years. Nevertheless, I hope you will

/agree

agree that the work must be accelerated so that by the time you see the President a precise and concrete offer can have been made to the Americans, in the areas where they have been seeking some movement by us. I am of course no expert on the technicalities of all this. But I should have thought that a mini-package might consist of one or more of the following: agreement to a system of 'double disapproval' of fares ~~(in practice the CAA are already substantially operating a 'double disapproval' regime)~~; opening up some of our regional airports to Transatlantic traffic; allowing some extra flights to People Express (the airline which the Americans see as a pioneer of low-cost travel and which has powerful friends in Congress); and possibly some other moves on summer capacity.

deleted.

4. On privatisation itself I confess that I am worried by the wide range of estimates which our professional advisers are giving about the likely cost of the private actions in the United States. I understand that Lord King's own judgement about the importance of the cases for privatisation has varied substantially over the last two weeks: he recently told the American Ambassador that in his own view privatisation could go ahead regardless of the civil suits. George Shultz argued that companies are being quoted on the New York Stock Exchange every day with legal liabilities much greater than those which face British Airways. The short answer to that is, of course, that the London Stock Exchange is a very different place. But I would be happier if our advisers were able to produce a clearer view, both in preparation for your meeting with the President and to help with the very difficult decisions we must take over the next weeks about the timing of privatisation and BA's handling of the civil suits.

5. In the medium and longer term I believe that we must continue to seek a comprehensive settlement with the Americans, which should include actions by them over private civil treble

/damage

damage law suits. But I think that we must accept that in their current state of mind they will neither act nor commit themselves to action on trebel damages. I believe that the position could change: many Americans share our view that in this respect the American legal system is defective. We should ensure that our action in the short term does not discourage those in Washington who will do what they can to help over the civil suits (not much in practice); nor spoil the chances for reform in the longer term.

6. You might therefore like to indicate to the President that this issue can be left on one side while officials on both sides of the Atlantic get on with negotiating other practical arrangements to benefit consumers, which is the goal of both governments.

7. I am copying this minute to the Chancellor of the Exchequer, the Secretary of State for Transport, Secretary of State for Trade and Industry and the Attorney General.

GEOFFREY HOWE

Foreign and Commonwealth Office
12 December 1984

P.01455

PRIME MINISTER

BA Privatisation and US Anti-trust Suits

The purpose of your meeting is to discuss the Secretary of State for Transport's minute of 10 December proposing that the privatisation of British Airways (BA) should be delayed, that this should be explained by uncertainties about the US anti-trust law and that the possibility should be pursued of a settlement with the Laker liquidator. The background was set out more fully in Mr Ridley's earlier minute of 4 December which was discussed at a meeting under the chairmanship of the Foreign and Commonwealth Secretary on 6 December. Mr Ridley is seeing Lord King tonight and he may wish to modify the assessment and proposals in his minute of 10 December in the light of that discussion.

2. You may also want to take the opportunity to have a word with those present about the handling of US/UK relations on civil aviation (on which you sent a message to President Reagan at the beginning of this week) in preparation for your forthcoming meeting with the President.

MAIN ISSUES

3. The main issues are as follows:

i. should a firm decision now be taken to delay the privatisation of BA beyond the mid-February date orginally planned?

ii. how should this delay be presented publicly?

iii. how should the US civil anti-trust cases be handled?

Timetable for privatisation

4. It is now common ground that, whatever course of action is pursued over the US civil anti-trust case, the timetable is already too tight for a successful flotation of BA in February. This was the unanimous view at the Foreign and Commonwealth Secretary's meeting last Thursday and (subject to tonight's meeting with Lord King) there is no sign that the situation has improved since then. You will be aware that Treasury Ministers are considering a possible alternative sale of assets within the current financial year.

5. It is not possible to judge how long the postponement might have to be. The earliest next available slot for BA might be April. Whether or not that date (or indeed any date in 1985) will be feasible must depend on the chosen course of action in respect of the anti-trust cases, and its likely prospects.

Presentation of the delay

6. The absence of any active steps to prepare for a February flotation of BA will soon become apparent in the City. The necessary preparations for an alternative asset sale will have the same effect. It would probably be desirable for the Government to volunteer some announcement about the postponement before Christmas, rather than let a City story develop. Mr Ridley was originally reluctant to refer to the anti-trust suits as a cause for delay on the grounds that this might weaken our case in the courts and in negotiations to achieve a settlement. He suggested last week that it might be preferable to cite the difficulty of agreeing with the Board of BA on the capital reconstruction, but the Treasury objected to this. Mr Ridley now proposes that the public explanation should be "the delay in clearing up the uncertainties about the application of anti-trust law". The Attorney General gave the impression at last Thursday's meeting that he would see no difficulty about a formula on those lines.

Mr Ridley may have more to say about presentation following his talk with Lord King. It will be necessary both to minimise the political damage domestically and to avoid weakening our position vis a vis the Laker liquidator and the US administration.

Options for handling the anti-trust cases

7. There are three main options for handling the anti-trust cases:

i. a comprehensive indemnity by the Government;

ii. a global settlement (ie involving not just BA but all the airlines concerned) with the Laker liquidator, leaving the remaining cases to be dealt with by insurance or in some other way;

iii. fighting the cases through the US courts, combined with a much tougher stand with the US administration.

8. The disadvantages of Option i. are obvious. A comprehensive indemnity would weaken BA's incentive to secure a tolerable outcome and would whet the appetite of the litigants. It would of itself increase the likely cost of resolving the suits. That cost could well be in excess of the proceeds of privatisation. This would have to be admitted at the time of privatisation and would expose the Government to severe public and Parliamentary criticism.

9. The problem about Option iii. is that it could delay privatisation for two years or more. To the extent that we chose not only to fight the cases but also to try and pressurise the US administration into legislative action on our behalf it could sour and disrupt the overall UK/US relationship. The Foreign and Commonwealth Secretary is seriously concerned about that risk.

10. Option ii. seems therefore to be the most promising but there are the following major snags:

a. It is not known how long it would take to achieve a global settlement. There may be a clearer estimate of this by the time of the meeting.

b. The cost for BA of a global settlement may be too high. The present estimate of at least £75 million is not attractive to the Treasury bearing in mind that the proceeds of privatisation against which it would have to be offset are likely to be in the range of £600-£900 million and there would remain the liabilities under the other anti-trust suits. The likely cost may also be better assessed by the time of your meeting.

c. Lord King asserted last Friday that, even if a settlement was reached with the liquidator, there would have to be an indemnity to cover the remaining suits. This view will need to be challenged. We shall in particular need to know whether there could be insurance against some at least of the liabilities and BA is exploring this.

11. Unless some new information is available by the time of your meeting which suggests that the global settlement option is not feasible, there seems no alternative but to continue to explore it, and to review the position again when we know where we stand.

US/UK relations on civil aviation

12. The letter from Mr Ridley's Private Secretary dated 10 December explains that the US Ambassador has now been told of our decision on low winter fares and our readiness to begin early talks on next summer's schedules. Mr Price appears to have given little encouragement that there will be further US moves to mitigate the anti-trust suits, claiming, on the basis of contacts with Lord King, that the financial effects on BA will be modest.

It is important to clear up the confusing signals to the Americans, with HMG expressing concern about triple damage suits, and Lord King playing down their significance

You will wish to take account of any further developments arising from the Foreign and Commonwealth Secretary's talk with Mr Schultz and you will no doubt be receiving an up-to-date brief before your meeting with President Reagan. Mr Ridley, who is becoming increasingly exasperated with the Americans on this matter, may press you to take a tough line with the President but you will wish to consider how best to proceed in the context of overall UK/US relations.

HANDLING

13. You will wish to ask the Secretary of State for Transport to speak about his proposals relating to the BA privatisation and the immediate handling of the US anti-trust suits. The Chancellor of the Exchequer and Financial Secretary, Treasury will have comments from the point of view of the privatisation programme generally. The Attorney General should be asked for advice on the legal aspects.

14. If there is discussion about relations with the US adminsitration on civil aviation matters, you will wish to invite views both from the Secretary of State for Transport and the Minister of State, Foreign and Commonwealth Office (Baroness Young).

CONCLUSIONS

15. You will wish to reach conclusions on:

i. whether the privatisation of BA should now be delayed beyond mid-February;

ii. whether this should be announced before Christmas and explained publicly by reference to uncertainties about the application of US anti-trust law;

iii. whether the possibility of a global settlement with the Laker liquidator should be pursued further, before final decisions are taken on the best way of handling the US anti-trust suits;

iv. (if appropriate) what line should be taken with President Reagan in Washington on civil aviation matters.

PLG

P L GREGSON

12 December 1984

PRIME MINISTER

12 December 1984

BA PRIVATISATION

We are riding a tiger and cannot now afford to get off. It is important that we are seen to ride the problems with confidence and resolution.

The business world and the press are aware that the Government and BA need to remove the uncertainty of the Laker-related liabilities and resolve the question of BA's capital structure before the final stage of privatisation. So far, there is little suggestion that a Spring launch is seriously in jeopardy. You cannot avoid risk by delay. Any hint that we are contemplating a significant postponement would be damaging. The inference would be that BA is more vulnerable to anti-trust than anyone had supposed. The US lawyers will scent blood. The pressures for more disclosure will mount and BCal could well become more seriously implicated.

As it is, the parties to the Laker liquidator's case evidently see this as a propitious moment to settle out of court. The liquidator and his lawyers sense that the pressures of BA privatisation will induce BA to make a generous settlement. Against the alternative of a drawn out and expensive battle through the courts, they would no doubt rather take the money and run. At the same time, their leverage against BA will be tempered by the desire to settle with the other airlines as well. All the airline managements

will want to get the troublesome matter behind them and concentrate on running airlines.

The cost of an out-of-court settlement is likely to take some swallowing. That cost will have to be judged not just in absolute terms, but in relation to the cost of the alternatives - which may well be higher.

A settlement with the liquidator will stop the flow of potentially damaging evidence which the class action lawyers and others contemplating anti-trust action can feed on. The scale of the residual liabilities should look less alarming once the settlement is out of the way. Insurance may still be possible. If not, Government will have to counter an indemnity for BA's liabilities arising from past anti-trust infringements which should have been obviated by Bermuda 2. BA do not think the indemnity could be geared to leave them with some liability and with it the incentive to fight the case strongly. Is this right? (BA are adept negotiators and sometimes need to have their bluff called.)

The immediate action items remain much as a week ago:

- Do not waver. Our posture to the outside world should be that we still have our sights set firmly on a Spring launch.

- Negotiate an out-of-court settlement with the Laker liquidator - weighing the cost of the alternatives very carefully before rejecting it.

- Be ready to cover the residual anti-trust liabilities by BA insuring, or HMG indemnifying BA, remembering that the buck stops at the Government in any event.

- Be ready rapidly to settle BA's capital reconstruction, bearing in mind that much of what we put in as additional equity should flow back through a higher market realisation. Transport are being tough negotiators. That's fine, but let's settle soon.

JOHN WYBREW

CONFIDENTIAL

CCNO

Prime Minister

BA PRIVATISATION AND US ANTI-TRUST SUITS

My minute of 4 December set out the problems for the BA privatisation presented by current and possible future anti-trust suits in the US courts. These were discussed at a meeting chaired by the Foreign Secretary on 6 December. The Attorney General, the Financial Secretary and the Parliamentary Under Secretary of State for Trade and Industry were also present.

The heart of the problem is that the Directors of BA and the Government must disclose in the prospectus all the information they have in their possession which could have a material effect on BA's financial prospects. While it is intolerable that our airlines should be subject to huge potential damages in the US courts for actions which we argue are legitimate under the Anglo/US Air Services Agreement, we have no means of removing these potential liabilities provided our airlines are to continue to trade in the US.

BA are fighting the liquidator's suit now. His maximum claim is $1bn. They believe that they have a good case, but no one can predict the outcome if, as seems certain in the absence of a settlement, it goes to a US jury. Fighting the case to the end would take a long time. Moreover, unless the case is stopped very soon, other anti-trust liabilities (both of BA and BCal), will be exposed by the US processes of document discovery. The only possible way to stop this discovery would be for all

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the defendants (including US, UK and European airlines) to reach a global settlement with the liquidator. BA are pursuing this possibility urgently.

When we discussed this, we were undecided as to whether BA should seek an early settlement, on acceptable terms, in respect of all defendant airlines, or whether it would be better for BA to fight the actions, with a prospect of success, but equally a prospect of substantial damages. The consequences to BA and BCal of a further disclosure of documents (which cannot be prevented if the case continues) is serious. Present estimates, which can only be tentative, are that the cost of a global settlement (including Corporation Tax) could be of the order of £100m, of which BA's share might be of the order of £75m. BA's negotiations continue, in order to determine the shape of a final package - and indeed whether a global settlement is possible - but the results will not be clearer until later this week, at the earliest.

Our plan has been to have the offer for sale in mid-February. To meet this, our advisers Hill Samuel need to take public steps now. My colleagues and I agreed that the risks of doing so in present circumstances would be far too great, since we can have no assurance that a satisfactory prospectus could be written. We agreed therefore that we must delay. The proceeds for sale cannot therefore be realised in the financial year 1984-85. The Financial Secretary is considering urgently whether other assets could be sold, to avoid disturbance to the Government's public expenditure plans.

BA are also facing a class action in the US courts, along with two US airlines. Their exposure to damages could be as high as $240m. This action is at an early

stage, and there is no possibility of a settlement at present. It would therefore have been necessary for the prospectus to refer to BA's potential liabilities arising from this and (subject to final legal advice from the Attorney General) to the possibility of other new actions against them in respect of violations of anti-trust law. BA are pursuing urgently the question of insuring against some at least of these liabilities.

Until very recently, BA had taken the firm position that, with the liquidator's case settled, the Directors would be able to sign a prospectus which dealt satisfactorily with the anti-trust cases. Lord King spoke to my Permanent Secretary on Friday to say that having taken further legal advice, he saw no way in which the Board could sign a prospectus in the foreseeable future unless the Government were prepared to give them a general indemnity against all liabilities which may arise from anti-trust actions, including the liquidator's suit, the present class actions, and any others. BA were unable to give my officials any indication of what the potential liability to the taxpayer might be as a result of the indemnity they have proposed. The indemnity would have to cover liabilities from actions from 1977 onwards. It therefore seems to me that the upper limit of the potential liability we would be assuming could be considerably greater than the proceeds we expect from privatisation.

For reasons I gave in my minute of 4 December, I find the idea of an indemnity very unattractive. I do not see how we could ask Parliament to approve it, particularly as we could not define its potential extent and could not adequately explain the reasons for it. It would, moreover, remove from BA any incentive to fight the cases and settle on the best possible terms. We are all agreed in recommending firmly against it.

I find the behaviour of the BA Board completely indefensible. Either they knew of the potential risks which they, and therefore the Government, were running and chose to conceal them, or they were negligent in not considering until well after the eleventh hour what liabilities they, as Directors, would have to disclose.

We shall now have to consider what courses are open to us. I think that an indemnity is most unattractive. There is a strong case for leaving BA to deal with the actions. We shall be able to see more clearly whether there is a middle way when we have a better assessment of the prospects and price of a settlement of the liquidator's action. I should have a clearer assessment of that later this week. We will also need to assess whether the remaining risks are insurable. I will report to you, and my other colleagues concerned, as soon as those further assessments can be made.

If the liquidator's case cannot be settled quickly on acceptable terms, they will have to continue to fight it. This will not only expose them to the possibility of other legal actions, but could also put at risk the future of BCal's US operations and possibly the airline itself. If such risks were in prospect, we should, in my view, be bound to take a much tougher stand with the US administration, including possible measures to recover any damages awarded or retaliatory action. But we are not at that point yet.

At present, we cannot assess how long it may be necessary to delay privatisation. I do not want to lose the momentum we have towards the earliest feasible offer for sale. If we have to delay we could justify that by saying that we had decided to wait until anti-trust problems had been cleared up.

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I propose:

(i) that I should be authorised to tell Lord King and Hill Samuel that we have decided to delay privatisation to allow time for the prospects of a settlement of the liquidator's suit to be fully explored, and any consequential decisions taken. I should wish to choose the time of telling them carefully, and would at the same time say publicly only that the delay in clearing up the uncertainties about the application of anti-trust law had led us to let the timetable slip;

(ii) that I should assess, as soon as possible, the prospects of a settlement with Lord King and my advisers and should report to you as soon as possible on that and on the options then open.

Copies of this minute go to the Foreign Secretary, the Chancellor of the Exchequer, the Secretary of State for Trade and Industry, the Attorney General, and to Sir Robert Armstrong.

Dinah Nichols
Private Secretary

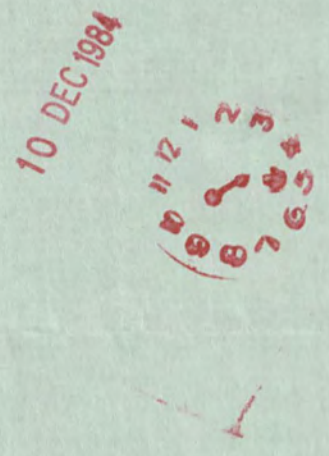
pp NICHOLAS RIDLEY
10 December 1984
(approved by the Secretary of State & signed in his absence)

CONFIDENTIAL

5F

AEROSPACE PT 3

future of BA



Ref. A084/3303

MR POWELL

In the margins of the meeting of Personal Representatives over the weekend, I was approached on the subject of civil aviation by my American colleague, Mr Allen Wallis, who (as you will remember) came to see the Prime Minister on this subject at Chequers last month.

2. Mr Wallis had been to see me in London on 7 December. My Private Secretary will have sent you a note of that meeting. On that occasion Mr Wallis was chiefly concerned to emphasise that there was no prospect that the United States Administration would legislate to abolish triple damage suits; and that, even if such legislation were introduced now, it would not remove the present threat, since the suits would arise from a period before any new legislation could take effect. He also pressed for some early move from our side, in response to the President's decision on the Grand Jury investigation. In our further conversation last weekend, Mr Wallis once again emphasised the significance of the President's decision. He could not remember any other case in which the President had intervened to prevent the law from taking its course. His decision had caused a lot of soreness in the Department of Justice, since they believed that the case against us was very strong. Nevertheless the President had acted in the wider political interests of the Anglo-American relationship and in the hope that his decision would enable matters to be moved along.

3. Mr Wallis's particular purpose in talking to me at the weekend was to tell me of a meeting which the United States Ambassador in London had had with Lord King of British Airways. It had become apparent from that meeting that Lord King did not share the Department of Transport's view about triple damage suits. British Airways was, according to Lord King, perfectly

able to continue to conduct its business in the United States without any change in the law in that respect. They also took a much less serious view than the Department of Transport appeared to take about the size of the damages to which they would be liable, if civil action was taken in the Laker case. In other words, it was clear that Lord King and his advisers in British Airways were taking a markedly different view on these matters from the Secretary of State for Transport and his advisers, and were perfectly ready to make this difference of view clear to the United States Ambassador.

4. I am not well versed in the details of this matter, but it certainly seemed to me, in the light of my conversation at the weekend, that we needed to get a better measure of understanding and co-ordination in the British position, before we took matters much further with the Americans.

RtA

ROBERT ARMSTRONG

10 December 1984

Covering CONFIDENTIAL

70 WHITEHALL, LONDON SW1A 2AS

01-233 8319

From the Secretary of the Cabinet and Head of the Home Civil Service

Sir Robert Armstrong GCB CVO

Ref. A084/3304

10 December 1984

Dear Derek,

UK/US Discussions in Civil Aviation

I attach a copy of a note of a meeting between Sir Robert Armstrong and Mr Allen Wallis, United States Under Secretary of State, and Mr Ray Seitz, Minister at the United States Embassy to discuss the Laker issue and the UK/US Discussions in Civil Aviation.

I am sending copies of this letter and attachment to Charles Powell, Len Appleyard, David Peretz and Callum McCarthy.

Yours

(R P Hatfield)
Private Secretary

Miss D A Nichols

Covering CONFIDENTIAL

Ref. A084/3290

NOTE FOR RECORD

Call by Mr Allen Wallis: Laker Dispute

Mr Allen Wallis and Mr Ray Seitz called at their request upon Sir Robert Armstrong on Friday 7 December to discuss the Laker issue.

2. Mr Wallis began by referring to his recent meeting with the Prime Minister when he had conveyed the President's decision to drop the criminal indictment against British Airways . That decision had been a very difficult one for the President: it ran contrary to his instinct not to interfere in the process of justice and to his strong belief in competition. It was the first time that the President had intervened in a criminal indictment and it had been especially difficult to intervene in this case as the Department of Justice considered that the evidence against the airline was very strong and the alleged offence was a very serious matter. The President had, of course, taken into account foreign policy considerations and his relationship with the British Prime Minister, but the main reason for his decision had been that he had been persuaded that dropping the indictment would make it easier to reach agreement on the liberalisation of air routes across the Atlantic and would thus be in accord with the purpose of anti-trust laws.

3. Sir Robert Armstrong added that the Prime Minister shared the President's beliefs in the role of law and in the importance of competition. She hoped that it would indeed be possible to reach agreement on a more liberal regime for trans-atlantic air routes and understood that negotiations to this end had been going well. The Prime Minister appreciated the President's action as easing the way for these negotiations.

4. Mr Wallis said that considerable progress had been made on the question of price liberalisation, on the basis of a "double veto", and that some progress had been made on the question of capacity, although this was proving more difficult because, for a number of reasons, the United States had at present a major competitive advantage. There had been two main stumbling blocks to the negotiations, the criminal indictment which had now been dropped, and the issue of "triple damages". There was, however, nothing the United States Government could do about this in relation to the Laker case and believed that the British negotiators had not fully understood the position. Although there was considerable sympathy in the United States for the repeal of the triple damages legislation (perhaps particularly because of its effects in medical cases) there was no possibility that the Senate would consider doing so at present, especially as the Laker issue was unresolved. In any case, if the legislation were to be repealed it would not affect the existing civil suits agains British Airways. He understood that the threat of very large damages in these suits affected the prospects for selling British Airways to the private sector but it was not uncommon in the United States for sales to go ahead in such circumstances: the possibility of impending damages could either be reflected in the sale price or an indemnity might be arranged.

5. Sir Robert Armstrong considered that there was no doubt that the triple damages issue remained a major problem. He had noted what Mr Wallis had had to say about this issue and would be reporting it. Nevertheless, the very large figure mentioned as possible damages would clearly have a serious effect on the prospects for privatisation. If the sale price had to be significantly lowered because of this the Government would be open to strong political criticism for selling off public sector assets too cheaply, and any reference to United States court cases would be treated merely as an excuse.

6. Continuing, Mr Wallis said that the triple damages issue was in any case irrelevant to the negotiations on liberalisation, which he hoped would be resumed before the President next saw the Prime Minister. As long as airlines operated within the law and used the procedures available to protect themselves problems would not arise: indeed the British Airways case was the only one since the law had been passed. Mr Seitz added that although the United States had orginally hoped that the negotiations would produce a broad revision and liberalisation of the regime they had scaled down their immediate expectations but it was important for the President that these negotiations should produce some substantial progress soon, even if the changes were initially on a provisional or trial basis.

7. In response to a comment by Sir Robert Armstrong that he had understood that the negotiations had been going well, Mr Wallis said that they had come to a halt, apparently because the United States had made it clear that there was nothing that they could do in the triple damages issue. This, however, should not have come as a surprise because he had explained this at his meeting with the Prime Minister. Although at an earlier stage in the negotiations there had been talk of the United States Government using its 'best efforts', there was in fact no possibility of stopping the civil suits, for the reasons he had explained. Mr Wallis added that there was no question of extraterritorality involved, as the civil suits related only to the sale of tickets in the United States.

8. Concluding the discussion, Sir Robert Armstrong said that he had noted the importance the United States attached to making progress on liberalisation, even if initially this had to be on a provisional basis. The British Government also wished to see greater liberalisation, with a framework which prevented the consequences which could arise from the extremes of competition,

and hoped that negotiations would resume shortly. He had noted what had been said about the triple damages issue but there was no doubt that this remained a problem.

9. In thanking Sir Robert for seeing him, Mr Wallis said that United States officials feared that the negotiations had reached a dead-end and stressed the political importance to the President of making progress in the near future.

R P HATFIELD

10 December 1984

CONFIDENTIAL

NBPM AT 10/12 CC NO

CP XI does not seem to require RTA's minute. AT 10/12

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

10 December 1984

Peter Ricketts Esq.,
PS/Foreign Secretary,
Whitehall,
London S.W.1

Dear Peter,

LAKER

The Foreign Secretary is seeing Mr Shultz tomorrow. He will wish to know of the discussion which my Secretary of State had with the United States Ambassador this morning. They met without others present but Mr Ridley has given me this account.

Mr Ridley told the Ambassador that we were now, following the discussions in Washington about the detailed arrangements, ready to agree in principle to low winter fares. The airlines would have to make their proposals and the detailed arrangements would need to be sewn up in Washington before a public announcement was made but he hoped that it would be possible to do this later in the week.

Mr Ridley went on to tell the Ambassador, in the strictest confidence, of the predicament which had been reached in relation to the privatisation of British Airways because of the civil suits. The alternatives for the Government were that privatisation should be postponed and the suits fought; or that the suits should be settled, but that settlement was also likely to call for some postponement. The costs of a settlement would not be trivial and could be expected to attract further political criticism.

Mr Ridley said that the United States had been asking for a concession by the United Kingdom, following the President's decision on indictments, which would go towards the overall settlement of this dispute. The winter fares decision should add to the favourable atmosphere - not least because untutored public opinion had seen the President's decision as likely to lead to progress on winter fares. Mr Ridley was ready for talks to begin early on next summer's schedules, but he warned that there would be difficulties for us on some points. Whichever course was followed in relation to the civil suits, it seemed likely that the delay in the sale of BA would need to become public fairly soon. The US Administration, in discussions with the Congress, could then point to this as the very substantial price to be paid (on either of the two courses followed) by the UK Government towards the resolution of the dispute, which would be entailed in their forbearing from escalating matters further on account of the intolerable position created by the private suits, as a manifestation of United States law to which the United Kingdom objected.

Mr Ridley said that he was keen that the negotiations on an overall package should be resumed, including the formulations which envisaged the removal of the treble damage suit. When the overall package of prospective agreement on the competition rules for airlines and liberalisation on the regulatory side was completed, it could be put on the table as being available as soon as the Congress was ready to legislate. Mr Ridley said that this course would offer a means for achieving an overall settlement of the remaining issues in dispute. He told the Ambassador that there were alternatives entailing an escalation of the dispute which he preferred not to consider.

The US Ambassador did not in the discussion depart from his previous line that British Airways had offended against United States law and must pay the price. He suggested that the cost for British Airways might be some $150 million (Lord King has recently been talking to the Ambassador and appears to have been the source of this figure). Mr Price suggested that this was not an unreasonable figure for British Airways to pay for their sins. Mr Ridley said that this line of argument was totally unacceptable to HMG.

Mr Ridley suggested to the Ambassador that he should not report widely on their discussion in Washington but should rather report fully to Mr Shultz.

Copies go to Andrew Turnbull (No 10), David Peretz (Treasury), Callum McCarthy (Trade and Industry), Richard Gardiner (Attorney General's Office) and to Sir Robert Armstrong.

Yours,

Miss D A Nichols
Private Secretary

E. R.

(1)

PRIME MINISTER

BA Privatisation

This has taken a turn for the worse. Last week it was hoped that, the criminal case having been lifted, an out of court settlement could be reached with the liquidator, and insurance taken out against future claims, for triple damages or from class actions.

We are now told - page 3 - that BA regard triple damage cases, present and future, as so harming the business that indemnities are required.

RTA has reported - see minute attached - that last week Lord King was playing down the problem of triple damages. I have asked the Department of Transport to confirm that Lord King has changed his mind. (They have now confirmed this)

I suggest a meeting is needed to sort out these problems and brief you ahead of your visit to Washington. This could be held after Cabinet on Thursday.

Agree?

AT Yes

A Turnbull

10 December 1984

CONFIDENTIAL

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OO WASHINGTON
GRS 456
CONFIDENTIAL
FM FCO 101200Z DEC 84
TO IMMEDIATE WASHINGTON
TELEGRAM NUMBER 2108 OF 10 DECEMBER
MIPT
MESSAGE FROM THE PRIME MINISTER TO PRESIDENT REAGAN.
1. THANK YOU FOR YOUR LETTER RECEIVED ON 27 NOVEMBER ABOUT RESOLVING THE OUTSTANDING DIFFERENCES IN THE CIVIL AVIATION FIELD AND FOR SENDING MR KENNETH DAM TO LONDON LAST WEEK TO EXPLAIN YOUR THINKING. AS YOU KNOW, I GREATLY WELCOMED YOUR COURAGEOUS DECISION ON THE GRAND JURY INVESTIGATION.
2. I FIRMLY ENDORSE YOUR VIEW THAT IT IS IN THE INTERESTS OF BOTH OUR COUNTRIES TO FIND SOLUTIONS TO THE PROBLEMS THAT HAVE ARISEN IN OUR CIVIL AVIATION RELATIONSHIP. WE SHARE A BASIC COMMITMENT TO DEVELOPING THE SYSTEM THAT REGULATES INTERNATIONAL CIVIL AVIATION IN A WAY THAT WILL ENSURE MORE COMPETITION ON THE HASIS OF FAIR TRADE. I CERTAINLY WANT TO MOVE FORWARD IN THAT AREA. BUT THE MORE WE LOOSEN THE TIES OF REGULATION THE MORE ESSENTIAL IT IS TO HAVE CLEAR AND MUTUALLY ACCEPTABLE RULES OF COMPETITION. AS YOU KNOW, WE ARE NOT ABLE TO ACCEPT THAT DOMESTICALLY APPLIED AND ENFORCED US ANTI TRUST LAW APPLIES IN THIS FIELD. FOR AN INDUSTRY THAT OPERATES INTERNATIONALLY THE COMPETITION RULES MUST BE JOINTLY AGREED AND ENFORCED OTHERWISE WE SHALL CONTINUE TO HAVE THE SORT OF PROBLEMS THAT HAVE ARISEN IN THE LAKER CASE.
3. I WAS GREATLY ENCOURAGCD AT THE END OF OCTOBER WHEN MY PEOPLE REPORTED THAT THE US NEGOTIATORS HAD SUGGESTED THAT WITHIN AN OVERALL SATISFACTORY PACKAGE THEY COULD CONTEMPLATE PROPOSING TO CONGRESS THE REMOVAL OF THE CIVIL TREBLE DAMAGE REMEDY FROM OUR BILATERAL AVIATION REGIME. FOR OUR PART WE INDICATED WE WERE WILLING TO ACCEPT FULL DISCLOSURE OF PRICE COORDINATION BETWEEN OUR AIRLINES, AND AN AGREED FRAMEWORK FOR ENFORCEMENT OF THOSE RULES BY THE AUTHORITIES

OF BOTH COUNTRIES. WE WOULD OF COURSE NOT BLOCK OR HINDER ENFORCEMENT BY YOUR AUTHORITIES UNDERTAKEN WITHIN SUCH A FRAMEWORK. I AM SURE THAT AGREEMENT ON THIS BROAD BASIS IS THE KEY TO INCREASING COMPETITION ON OUR AIR ROUTES.

4. WE WERE THEREFORE VERY DISAPPOINTED TO HEAR FROM MR DAM THAT THE US GOVERNMENT DID NOT NOW FEEL ABLE FOR THE TIME BEING TO PURSUE THE DISCUSSION OF THE REMOVAL OF THE TREBLE DAMAGE REMEDY. I AM AFRAID THAT THIS WILL SERIOUSLY UNDERMIND THE STRENUOUS EFFORTS WE ARE MAKING TO MEET YOUR WISHES ON SOME OF THE OTHER POINTS IN THE PACKAGE. I DO HOPE THAT WE CAN NOW GIVE THESE NEGOTIATIONS THE NEW IMPETUS WHICH IS ESSENTIAL IF WE ARE TO LOOSEN THE REGULATORY FRAMEWORK. I HAVE TOLD MY OFFICIALS TO BE READY TO CONTINUE NEGOTIATIONS URGENTLY AND CONSTRUCTIVELY.

5. IN THE MEANTIME, AS MR RIDLEY HAS TOLD AMBASSADOR PRICE, WE HAVE BEEN ABLE TO FIND A WAY TO APPROVE LOW WINTER FARES. I HOPE THAT THIS CAN BE ANNOUNCED LATER IN THE WEEK WHEN OUR PEOPLE AND YOURS HAVE SETTLED THE DETAILS.

HOWE

US ANTI-TRUST ACTION AGAINST BRITISH AIRLINES

LIMITED

MAED
NAD
NEWS D
ERD
PLANNING STAFF
LEGAL ADVISERS
PS
PS/MR RIFKIND
PS/MR RENTON
PS/PUS
MR BRAITHWAITE
MR O'NEILL
MR DAVID THOMAS

ADDITIONAL DISTRIBUTION
US ANTI-TRUST ACTION AGAINST BRITISH AIRLINES

FILE

VC

CONFIDENTIAL

10 DOWNING STREET

From the Private Secretary

10 December 1984

Dear Dinah,

UK/US DISCUSSIONS ON CIVIL AVIATION

Thank you for your letter of 7 December enclosing a draft message from the Prime Minister to President Reagan. We subsequently discussed a possible addition to this, dependent upon progress over winter fares during the weekend.

BF

The Prime Minister saw and approved the draft over the weekend with some further minor amendments. I enclose the approved version and should be grateful if arrangements could be made to have it delivered as soon as possible.

I am copying this letter and enclosure to Len Appleyard (Foreign and Commonwealth Office), David Peretz (HM Treasury), Callum McCarthy (Department of Trade and Industry), Henry Steel (Attorney General's Office) and Richard Hatfield (Cabinet Office).

Yours sincerely,

C.D. POWELL

Miss D.A. Nichols,
Department of Transport.

dg

CONFIDENTIAL

MESSAGE FROM THE PRIME MINISTER TO PRESIDENT REAGAN

Thank you for your letter received on 27 November about resolving the outstanding differences in the civil aviation field and for sending Mr. Kenneth Dam to London last week to explain your thinking. As you know, I greatly welcomed your courageous decision on the Grand Jury investigation.

I firmly endorse your view that it is in the interests of both our countries to find solutions to the problems that have arisen in our civil aviation relationship. We share a basic commitment to developing the system that regulates international civil aviation in a way that will ensure more competition on the basis of fair trade. I certainly want to move forward in that area. But the more we loosen the ties of regulation the more essential it is to have clear and mutually acceptable rules of competition. As you know, we are not able to accept that domestically applied and enforced US anti trust law applies in this field. For an industry that operates internationally the competition rules must be jointly agreed and enforced otherwise we shall continue to have the sort of problems that have arisen in the Laker case.

I was greatly encouraged at the end of October when my people reported that the US negotiators had suggested that within an overall satisfactory package they could contemplate proposing to Congress the removal of the civil treble damage remedy from our bilateral aviation regime. For our part we indicated we were willing to accept full disclosure of price coordination between our airlines, and an agreed framework for enforcement of those rules by the authorities of both countries. We would of course not block or hinder enforcement by your authorities undertaken within such a framework. I am sure that agreement on this broad basis is the key to increasing competition on our air routes.

We were therefore very disappointed to hear from Mr. Dam that the US Government did not now feel able for the time being to pursue the discussion of the removal of the treble

damage remedy. I am afraid that this will seriously undermine the strenuous efforts we are making to meet your wishes on some of the other points in the package. I do hope that we can now give these negotiations the new impetus which is essential if we are to loosen the regulatory framework. I have told my officials to be ready to continue negotiations urgently and constructively.

In the meantime, as Mr. Ridley has told Ambassador Price, we have been able to find a way to approve low winter fares. I hope that this can be anounced later in the week when our people and yours have settled the details.

cc PC

(1)

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB
01-212 3434

Prime Minister. (1)
It is surely better to add the point about low winter fares to your message, once it is the only good news which we have to give him at this stage.
Agree message with this addition (which is acceptable to the Department of Transport)?
The last para needs to be better put
CDP 7/XII

C D Powell Esq
10 Downing Street
LONDON
SW1

7 December 1984

Dear Charles,

UK/US: DISCUSSIONS ON CIVIL AVIATION

You wrote to me on 27 November seeking a draft reply to the message to the Prime Minister from President Reagan which you had received that day. You may have seen that Sir Oliver Wright's views have been sought on a draft reply which was before Ministers yesterday evening when the small group under the chairmanship of the Foreign Secretary considered the general handling of the aviation dispute with the United States and its impact on the privatisation of British Airways.

Ministers agreed that the Prime Minister should be recommended to reply to President Reagan as soon as possible. The draft enclosed is fundamentally that recommended by Sir Oliver Wright with some small drafting amendments agreed between our officials and those of the FCO. Mr Ridley is content with the draft, and I understand that the Foreign Secretary will be considering it overnight. I understand the Prime Minister wishes to send it tomorrow, so that it is received well before Mr Shultz's visit on Tuesday.

Monday K
CDP

Mr Ridley indicated in his minute of 4 December to the Prime Minister that he thought it appropriate to clear the remaining obstacles to the approval of low fares this winter. Ministers endorsed this in principle at the meeting yesterday. There will be some residual risk of a new private anti trust suit but the contemplated formal exchanges with the US Government will reduce this to a low level (and will themselves be a useful precedent for so long as the basic dispute remains unresolved). No mention is made of the low fares in the message to President Reagan, not least because it seems inappropriate for the Prime Minister and the President to correspond on the minor details of the negotiation. The US side, however, know that we are actively pursuing the question and, provided that the remaining points have been cleared we should aim to say something positive about the fares at the time that the Prime Minister's message is delivered.

When Ministers discussed this yesterday they felt we should have to await reactions to the message and our decision on the low fares before deciding how to pursue further the question of future arrangements.

Copies go to the Private Secretaries to the Foreign Secretary, the Chancellor of the Exchequer, the Secretary of State for Trade and Industry, the Attorney General and to Sir Robert Armstrong.

Yours,
Diana.

Miss D A Nichols
Private Secretary

JDACH

DRAFT MESSAGE FROM THE PRIME MINISTER
TO PRESIDENT REAGAN

Dear Ronald

~~Many thanks~~ for your letter received on 27 November about resolving the outstanding differences in the civil aviation field and for sending Mr Kenneth Dam to London last week to explain your thinking. As you know, I greatly welcomed your courageous decision on the Grand Jury investigation.

I firmly endorse your view that it is in the interests of both our countries to find solutions to the problems that have arisen in our civil aviation relationship. We share a basic commitment to developing the system that regulates international civil aviation in a way that will ensure more competition on the basis of fair trade. I ~~am~~ certainly ~~willing~~ wanting to move forward in that area. But the more we loosen the ties of regulation the more essential it is to have clear and mutually acceptable rules of competition. As you know, we are not able to accept that domestically applied and enforced US anti trust law applies in this field. For an industry that operates internationally the competition rules must be jointly agreed and enforced otherwise we shall continue to have the sort of problems that have arisen in the Laker case.

I was greatly encouraged at the end of October when my people reported that the US negotiators had suggested that within an overall satisfactory package they could contemplate proposing to Congress the removal of the civil treble damage remedy from our bilateral aviation regime. For our part we indicated we were willing to accept full disclosure of price coordination between our airlines, and an agreed framework for enforcement of those rules by the authorities of both countries. We would of course ~~agree~~ not ~~to~~ block or hinder enforcement by your authorities undertaken within such a framework. I am sure that agreement on this broad basis is the key to increasing competition on our air routes.

This is very disappointing and we will so inform our colleagues.

We were therefore very disappointed to hear from Mr Dam that the US Government did not now feel able for the time being to pursue the discussion of the removal of the treble damage remedy. This ~~undercuts~~ seriously ~~the efforts we were making to meet you on some of the other points in the package.~~ I do hope that we can now give these negotiations the new impetus which is essential if we are to loosen the regulatory framework, ~~in this area.~~ I have told my officials to be ready to continue negotiations urgently and constructively.

In the meantime, as Mr. Ridley has told Ambassador Price, we have been able to find a way to approve low winter fares. I hope that this can be announced later in the week when our people and yours have settled the details.

I am afraid that this will seriously undermine the serious efforts we are making to meet your wishes on some of the other points in the package.

Aerospace - CAA review 43

File

CONFIDENTIAL

MINUTES of a Meeting of Ministers held in Conference Room A, Cabinet Office, on THURSDAY 6 DECEMBER 1984 at 6:45pm

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PRESENT

The Rt Hon Sir Geoffrey Howe QC MP
Secretary of State for Foreign and Commonwealth Affairs (In the Chair)

The Rt Hon Nicholas Ridley MP
Secretary of State for Transport

The Rt Hon Sir Michael Havers QC MP
Attorney General

Mr John Moore MP
Financial Secretary, Treasury

Mr Alexander Fletcher MP
Parliamentary Under-Secretary of State, Department of Trade and Industry

ALSO PRESENT

Mr A I Aust
Foreign and Commonwealth Office

Mr R J O'Neill
Foreign and Commonwealth Office

Mr R H Wilson
H M Treasury

Mr R J Ayling
Department of Trade and Industry

Mr J M Healey
Department of Trade and Industry

Mr D Holmes
Department of Transport

Mr W M Knighton
Department of Transport

Mr J Gardner
Law Officers' Department

SECRETARIAT

Mr P L Gregson

Mr M S Buckley

Mr N P F Brind

SUBJECT

BRITISH AIRWAYS PRIVATISATION, THE LAKER SUITS, AND NEGOTIATIONS WITH THE UNITED STATES ADMINISTRATION ON FUTURE ANTI-TRUST ARRANGEMENTS.

BRITISH AIRWAYS PRIVATISATION, THE LAKER SUITS, AND NEGOTIATIONS WITH THE UNITED STATES ADMINISTRATION ON FUTURE ANTI-TRUST ARRANGEMENTS.

The meeting discussed the privatisation of British Airways PLC (BA), the suits brought by the liquidator of Laker Airways, and current negotiations with the United States Administration on future anti-trust arrangements in the context of civil aviation. They had before them minutes of 4 December from the Secretary of State for Transport to the Prime Minister, and a letter of the same date from the Private Secretary to the Secretary of State for Transport to the Private Secretary to the Foreign and Commonwealth Secretary with the draft of a message from the Prime Minister to the United States President.

British Airways Privatisation

THE SECRETARY OF STATE FOR TRANSPORT said that there were two main problems: the problem of the implications for the privatisation of BA of suits brought in the US courts by the liquidator of Laker Airways for damages arising from alleged breaches of anti-trust legislation; and current negotiations with the US authorities on future arrangements to remove from the scope of civil anti-trust suits services covered by air services agreements between the US and the United Kingdom. The problems were connected in that solutions to them should be mutually supportive.

There were four possible ways of tackling the 'Laker' suits.

(i) It would be possible to seek a settlement with the liquidator, ideally covering both BA and the other nine airlines who were co-defendants. This could possibly cost about £100 million, after allowing for corporation tax liabilities; BA's share might be about £65 to £70 million.

(ii) It would be possible to fight the case in the US courts. Although BA were advised that they had good chances of success, the outcome was unpredictable. The Government's merchant bank advisers on the prospective flotation of BA, Hill Samuel, had advised that the risk, which would naturally have to be disclosed in the prospectus, would make it impossible to float BA until the action was decided.

(iii) It would be possible to give BA an indemnity. This would effectively admit liability; and no upper limit could be set to the Government's commitment. He could not recommend it to his colleagues.

(iv) It would be possible to act on a high political level by, for example, announcing the Government's intention to recover any damages awarded by the US courts against UK airlines by levying a tax on United States aircraft landing in this country, or by legislating to forbid UK airlines to pay damages awarded in civil anti-trust suits against actions which were legitimate under our Air Services Agreement with the US.

A further difficulty was that there was a consolidated class action in the US courts against BA alleging loss from higher airfares after the collapse of Laker Airways in consequence of an alleged conspiracy between BA and other airlines. The liability from class actions of this sort was unpredictable; and further such actions could arise at any time. It might be possible to deal with them, in the context of the flotation of BA, by commercial insurance, perhaps coupled with some form of Government indemnity. How the liquidator's action was handled would have implications for the conduct of, and the prospects of success in, the class actions. Decisions were urgent. Hill Samuel had said that they needed to know that day which course was to be taken if the possibility of flotation in mid-February was to be kept open.

In discussion, the following main points were made.

(a) The chances of being able to float BA in mid-February seemed very slight. The only certain way of achieving it was to give an indemnity to BA in respect of the liquidator's action. This had serious disadvantages, as the Secretary of State for Transport had pointed out. It might be possible to reach a negotiated settlement with the liquidator; but there was no certainty of this. Moreover, the liquidator's negotiating position would be stronger if he knew that the Government, or BA, was negotiating against a tight deadline.

(b) The class actions were a separate problem. It might be easier to deal with them by commercial insurance, perhaps supplemented by an indemnity. However, such an indemnity would suffer from several of the disadvantages attaching to an indemnity against the liquidator's action. It would also be open-ended, since further actions could be started at any time.

(c) If flotation was delayed, it could not take place before the following financial year. In order to keep to the Government's published expenditure plans it would be necessary to sell other assets. Treasury Ministers would wish to discuss the position with the Secretary of State for Transport, and perhaps other colleagues. These developments were market-sensitive, and should be kept strictly confidential.

(d) However, it would soon become known if the Government decided to defer the flotation of BA; and the delay would have to be explained. This might be done by reference to the difficulties of resolving a difference of view between the Board of BA and the Government over the amount of the sale proceeds which BA should be allowed to retain in order to strengthen the Company's balance sheet. But doing so would have drawbacks. Equally, it would be undesirable to say anything which implied that BA or the Government conceded liability in the civil actions in the US.

It should not be impossible to devise an explanation based on the unavoidable uncertainty attached to the actions, and the inadvisability of attempting flotation while such uncertainty existed.

(e) Although it would strengthen the negotiating position against the liquidator if the Government was not committed to early privatisation of BA, there were still good reasons for seeking a quick settlement. Not only would this remove one of the main obstacles to privatisation. There was also the point that the longer legal proceedings continued, the greater the risk of matters coming to light which would be seized on by litigants as grounds for further action in the US courts.

(f) The advice given by the Government's financial and legal advisers had largely been based on the assumption that flotation would take place in mid-February. If that assumption was no longer valid, the advice might well be substantially different. A fundamental reappraisal of the position was needed.

THE FOREIGN AND COMMONWEALTH SECRETARY, summing up this part of the discussion, said that the meeting agreed that the course of indemnifying BA against the liquidator's action must be ruled out. He would also have serious reservations about the wisdom of pursuing the fourth option described by the Secretary of State for Transport, that of politicising the issue. Subject to any further considerations that might emerge in the next

24 hours, the meeting agreed that the risks attached to an attempt to maintain the timetable for a flotation of BA in mid-February were too great, and that some delay must be accepted. In these circumstances, the best solution seemed likely to be an early settlement with the liquidator of Laker Airways on reasonable terms, and in respect of all the defendant airlines, not only BA. However, this might not be easy to achieve. The options of a settlement for BA alone, and of fighting the liquidator's action in the US courts could not be ruled out. There was also the problem of the class actions, on which the meeting had reached no firm conclusions. The Secretary of State for Transport should urgently reappraise the options in the light of the discussion and report his conclusions as quickly as possible to the Prime Minister and the other colleagues concerned, including the Secretary of State for Trade and Industry. All those present, and their advisers, should bear in mind the need for strict confidentiality.

The Meeting -

1. Took note, with approval, of the Foreign and Commonwealth Secretary's summing up of this part of their discussion.

2. Invited the Secretary of State for Transport to report to the Prime Minister on the lines indicated by the Foreign and Commonwealth Secretary.

Negotiations with the US Authorities

THE SECRETARY OF STATE FOR TRANSPORT said that after President Reagan's decision to instruct the American Department of Justice to withdraw the criminal anti-trust investigation of BA, the US negotiators had indicated that they expected this country to make some reciprocal gesture of good will. However, there were four matters on which we regarded ourselves as aggrieved parties: criminal actions in anti-trust arising from the past; the continuing possibility of such actions; civil actions in anti-trust arising from the past (especially the suits involving BA); and the continuing possibility of such actions. President Reagan had removed only the first of these, which was the least important in financial terms. Against that, the US negotiators had sought to draw back from their earlier proposal to promote legislation to remove civil anti-trust treble damage suits from services covered by the Air Services Agreement. In these circumstances, it was hard to see why we should make any reciprocal gesture, let alone concede, as the US negotiators appeared to envisage, tariff liberalisation, reductions in restrictions of capacity, and a resolution of the 'Winter fares' problem. Nevertheless, to encourage the US authorities to adopt a more forthcoming attitude, he thought it would be right to approve new fares for the coming Winter. In order to improve the chances for wiser counsels to prevail in the US Administration, it would be desirable for the Prime Minister to send a message to President Reagan. His Private Secretary's letter of 4 December set out a possible draft.

In discussion, the following main points were made.

(g) Although President Reagan's intervention in the criminal anti-trust action had been described as 'courageous', it had in fact been well received by public opinion in the United States. Nor did it have any bearing on past or future civil anti-trust actions. It provided little justification for concessions of substance on the part of the UK.

(h) Moreover, although there were some concessions which the US Administration hoped to secure from us, in particular a limitation on the use of powers under the Protection of Trade Interests Act, our negotiating position was not strong. We could not afford to make substantial concessions without a commensurate return. It was essential to remove the threat of civil anti-trust actions in respect of legitimate activities under the Air Services Agreement.

(i) A settlement of the 'Winter fares' problem could be conceded without prejudicing our interests. We might also offer to discuss new Summer schedules. But it would be difficult to go further.

THE FOREIGN AND COMMONWEALTH SECRETARY, summing up this part of the discussion, said that the meeting agreed that it would be right to offer the US authorities a reciprocal gesture of goodwill which did not make concessions of substance: the most promising possibility was to offer to settle the 'Winter fares' problem.

This should be done as quickly as possible. The Prime Minister should also be advised to send a message as soon as possible to President Reagan. This message should be brief, and should concentrate on the point that the US negotiators had withdrawn their previous offer regarding civil anti-trust actions, a point of cardinal importance to the UK.

The Meeting -

3. Invited the Secretary of State for Transport:

(i) to consider, in consultation with the Foreign and Commonwealth Secretary, what gesture of goodwill could be offered to the US authorities, on the basis described by the Foreign and Commonwealth Secretary in his summing up;

(ii) to submit to the Prime Minister the draft of a message which she might send to President Reagan.

Prime Minister (2)

Although I do not recommend you to intervene before Sir Geoffrey's meeting, you may like to see this. I suspect it is right.

cc. Laker: Legal Procedure
Mark 83

AT 5/12

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(2)

PRIME MINISTER 5 December 1984

BA PRIVATISATION AND THE LAKER SUITS

Geoffrey Howe's meeting tomorrow will be faced with complex US legal problems of uncertain dimension and an array of unpalatable options - including the possibility of a nasty dust-up with the US Government. It would be helpful if you could encourage him to concentrate on first things first; it is easier to see the wisdom of the next step or two than contemplate the journey as a whole.

Delaying BA's launch into the private sector will not only cost money in the current financial year, but is also likely to increase the risk of losing the Laker civil suits and of damaging the Government's wider relations with the US; the press are likely to read the delay as implying some guilt whatever we say. There seems a fair prospect that the airlines defending the case raised by the Laker liquidator could rapidly conclude an acceptable out-of-court settlement. (The fact that the liquidator's lawyer is haggling for his reward is encouraging.) That being so, we can still achieve the February deadline for the launch.

The immediate plan of action should, therefore, be:

1. Conclude out-of-court settlement with the Laker liquidator.

2. Meanwhile, expedite legal advice on how best to cover the Laker-related class actions (qualification in prospectus, BA takes out insurance, HMG indemnifies BA in respect of liabilities which should have been obviated by Bermuda 2).

3. Also in parallel, expedite legal advice on whether other possible anti-trust actions (not related to Laker) can be dealt with satisfactorily in the prospectus.

4. And simultaneously conclude negotiations with BA on capital reconstruction prior to privatisation.

We may be thwarted on any of these, and will then have to consider fallbacks. The greater threat lies in not resolutely grasping the nettle and pressing ahead for the February launch. Importantly, BA's management still have the conviction that they can achieve this.

JOHN WYBREW

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PRIME MINISTER

BA PRIVATISATION AND THE LAKER SUITS

1. We need to decide very quickly how to handle the British Airways (BA) flotation in view of problems arising from civil suits against them in the US courts. President Reagan's intervention to prevent any criminal indictments on matters under investigation by the Department of Justice was helpful, but neither it nor the current talks with US departments will affect cases concerned with alleged anti-trust violations in the past.

The current civil suits are:

(i) the Laker liquidator's case;

(ii) the current class action.

The attached note by officials (Annex A) summarises the complications and uncertainties of these cases. It shows that there is a possibility of further class actions which might arise from evidence revealed through the process of discovery in the US courts, encouraged by the widely reported and damaging statements by Department of Justice officials immediately after President Reagan's intervention.

2. The Government as vendor of the shares in BA plc must disclose any information in its possession which would falsify any information already in the prospectus and correct any conclusion or inference which could otherwise reasonably be drawn from the prospectus. We shall therefore need to make a considered judgment (about which I am separately consulting the Attorney General) about what it is necessary to disclose, and whether we can proceed with the flotation on the basis of that disclosure.

3. BA's US legal advisers say that they should win the liquidator's case and the class action as currently constituted.

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But they cannot give any assurance that this will be the outcome. The case will not come to trial before summer 1985 and the class action a good deal later. Meanwhile a statement in the prospectus must point to the risks both as to the outcome and to the quantum of damages which a jury might award against BA. Hill Samuel and Lazards have considered a draft (annex C) for the prospectus on these lines, and advise that such a statement would not allow a successful flotation.

4. In addition there is the possibility that the class action might be further amended or further class actions begun, which could generate other potential liabilities. BA's advisers think that such risks are remote, but from the knowledge in the Government's possession, they cannot be ruled out.

5. Under the timetable for a flotation in mid-February (the key dates for which are set down in annex B), Hill Samuel will need within the next few days to issue invitations to the marketing seminars beginning on 7 January. I must decide quickly whether this timetable can be adhered to. Once the invitations have been issued it will be difficult to abort the sale without an adverse reaction in the stockmarket. If it became known that the Laker litigation was the reason for postponement, it would be very damaging to BA's chances of success in the US civil suits.

Possible settlement

6. More than 90 per cent of US civil anti-trust actions are settled out of court because, with high legal costs, the risks of losing are too high. The best solution to the present problems would be a global settlement of the liquidator's suit by all ten defendant airlines, and a settlement of the class action. The former could not be achieved within a reasonably short period, and the class action has not yet reached the point where settlement could be considered.

7. BA are urgently exploring the possibilities of an individual settlement with the liquidator. They believe that such a settlement would greatly improve the chances of a successful flotation, particularly if BA were to insure against liabilities from the class action. It would, however, leave the rest of the liquidator's case still active and it would remain possible for documents to be released which could give rise to further class actions against BA. I shall separately be consulting the Attorney General about what would have to go into the prospectus if BA settled on this basis, and will need to consult Hill Samuel about whether that disclosure would allow a successful flotation.

8. It is extremely difficult to estimate the cost to BA of settling. The liquidator has mentioned eight figure dollar sums. BA tell me that insurance against the liability arising from the liquidator's action would not be feasible. BA consider that insurance against liability under the class action may be possible, but this has yet to be firmly established.

9. Any settlement will take time to achieve. Until a settlement, at least by BA, of the liquidator's suit has been confirmed we cannot safely proceed with flotation. Therefore some delay in the timetable may be inevitable unless we take the exceptional course of insulating BA against the risks.

Insulating BA

10. For this option to be effective, the Government would need to undertake to BA to pay the airline any sum which it is, or becomes, liable to pay as a result of the existing actions and any other anti-trust actions which are brought in relation to anti-trust violations before flotation. It can be argued that the cost to the Government of giving an indemnity might not be much greater than the Government's present exposure while BA remains in the public sector, but I find this option very unattractive, because:

(a) no upper limit could be set to the Government's contingent liability:

(b) it would remove from BA any incentive to fight the cases or settle economically. Further if HMG, in effect, took on the defence of the cases, it would be more likely that the US courts would view our action to block UK documents under the Protection of Trading Interests Act as a matter of expediency rather than principle. That could make the cases harder to fight;

(c) there would be problems in the coverage of an indemnity. To enable a satisfactory prospectus to be published, an indemnity would need to cover all potential treble damage liabilities. We could not confine it to liabilities from behaviour by BA which we argue is legitimate under Bermuda 2;

(d) politically it would be difficult not to indemnify BCal also, although the case against BCal is on different grounds.

11. An indemnity of this kind would be different in nature from the guarantee enshrined in the Memorandum of Understanding (MOU) between British Airways plc and me. Under that, the Government stands behind the company and will not allow it to default. This guarantee will lapse on flotation. An indemnity insulating BA from anti-trust liability would, on the other hand, have to be honoured by the Government irrespective of BA's own ability to pay. The one merit of this option would be that it would allow a marketable prospectus to be written.

Nullifying the effects of the suits

12. The courses of action described above are extremely unpalatable. They involve either BA or the Government paying substantial sums to meet liabilities under US anti-trust laws, which we firmly believe should not apply to matters governed

by our air service agreement with the USA (Bermuda 2). This suggests that the right course in principle would be to take powers to prevent BA (and perhaps BCal) from paying any damages awarded against them by the US courts in anti-trust suits. But as that would probably lead to seizure of our airlines' assets in the USA, we should also need to take powers to seize a comparable amount of the assets of US airlines here.

13. I am advised that to be able to enact (or at least use) such legislation without a breach of international law, we should need to demonstrate that permitting the continuation of the private suits was a breach of Bermuda 2 and that the action proposed by HMG was a reasonable and proportionate response. Arbitration under Bermuda 2 is the proper remedy (although this is uncertain both as to its timing and result). Since the US have taken the position that there has not been a breach of Bermuda 2, and there has been ample time for HMG to take the matter to arbitration, I am advised that retaliatory action could not be justified under international law as being a reasonable and proportionate response.

14. Whatever the legal arguments, retaliatory action would also cause a row with the US. Though the US Government might be brought to understand our position of principle, we could not rely on their being willing or able to back down to what they would see as an attack on their system - still less on their being able to carry legislation in the Congress even if they were willing to propose it. At best it would take time to resolve the deadlock, and - given the uncertainties for Anglo-US air services in the meantime - privatisation of BA would be held up.

15. If, for these reasons, we adopt either a settlement or an indemnity to enable privatisation to go ahead, the dilemma is how to reconcile acquiescence in the application of anti-trust laws for the past with maintaining our position of principle from which to negotiate arrangements for the future.

16. I am minuting you separately on what tactics we should use to make progress with the US government towards removing the possibility of treble-damage suits from our civil aviation relationship. I do not rule out threatening tougher action if that proves necessary. And if we decide that we have to acquiesce in the application of US anti-trust law in the present suits, to enable privatisation to proceed, we should make it clear to the US government that this is a political response to President Reagan's decision to stop the Department of Justice indictment, which does not alter our position of principle.

Conclusion

17. (i) the only option which we could be sure would be consistent with keeping to the present timetable of flotation in mid-February would be to give BA a wide indemnity against liabilities arising from civil anti-trust suits. This is open to the objections in paragraph 11;

(ii) we may just be able to keep to the present timetable, if BA can reach an early settlement with the liquidator at a reasonable cost; and can insure against liabilities arising from the class action. But it would not be safe to take public steps towards the flotation until this solution has been secured and the Government's obligations in relation the prospectus have been completely clarified (paragraph 8). It may well be necessary to defer the flotation beyond the end of the current financial year, we would have to explain the delay by referring to the difficulty of settling BA's capital structure with Lord King;

(iii) the most logical solution is to threaten retaliatory action against US airlines in the event of damages being awarded against BA. It would have widespread consequences for Anglo-American relations. It maintains our principles but would not offer a safe route to early privatisation.

18. Copies of this minute to go to the Foreign and Commonwealth Secretary, the Chancellor of the Exchequer, the Secretary of State for Trade and Industry, the Attorney General and to Sir Robert Armstrong.

Dinah Nicholls
Private Secretary

pp NICHOLAS RIDLEY
4 December 1984

(approved by the Secretary of State & signed in his absence)

BA'S EXPOSURE TO US ANTI-TRUST LAWS

1. The contents of this document are highly sensitive, particularly those passages in square brackets, and should on no account be disclosed to anyone outside HMG.

2. HMG as vendor of the shares in BA Plc has a duty of good faith to the investing public. It must disclose any information in its possession which would correct any conclusion or inference which could otherwise reasonably be drawn from the prospectus.

3. Thus a dilemma is created. If HMG knows that there is a hidden potential liability which may in the course of time see the light of day (and is material to the conclusion to be drawn about the company's prospects), that should be disclosed. Yet the very disclosure may turn a potential liability into an actual one. The only way out of this dilemma is not to sell shares whilst the potential liability exists, or to disclose it and indemnify the company.

4. Although the US Government's decision not to pursue criminal indictments in relation to the matters under investigation is a positive factor, it does not remove the underlying problem of BA's existing potential civil (or other criminal) liabilities under US anti-trust laws.

5. In the existing Laker liquidator's action the sum of 1 billion US dollars is claimed from BA and other defendants (any one is liable for the full amount awarded without any right of contribution from the others). We are advised that the current assessment is that there is a 50/50 chance of success by the liquidator and the damages awarded could be of the order requested. Whilst BA and its US legal advisers believe they should win the case they do not demur from the proposition that no assurance can be given as to the jury's verdict. If this assessment is correct it would in itself

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be a damaging enough statement to put in a prospectus, and could require the creation in the accounts of a contingency reserve to cater for such potential liability (which would itself be relevant to the company's capital structure and debt/equity ratio). A statement of this nature would certainly greatly encourage the liquidator.

6. It follows from the above that the liquidator's case should be settled by the end of January if the present timetable is to be met. Yet that is not solely within our, or BA's, control. The liquidator may be asking for too much. /Further, we understand that his price depends upon a condition of a settlement which is not within BA's power to grant, namely the release of the UK documents blocked by HMG under the Protection of Trading Interests Act. Those documents, whilst equivocal in terms of the conspiracy alleged in the action, do disclose breaches of anti-trust./ Without a settlement, there is no possibility of the case being completed by mid-February.

7. This is currently a consolidated class action against BA alleging loss from supposedly higher air fares after the demise of Laker in consequence of the alleged conspiracy. This is at an early stage and it is unrealistic at this point in time to quantify a possible liability, although BA's US lawyers calculate that the maximum currently claimed could be 240 million US dollars but that a more realistic assessment is that maximum potential liability ranges from 12-90 million dollars (depending upon which allegations are successful). We are advised that Judge Greene is likely to certify that an appropriate class exists for the purposes of US law and we have no reason to believe that the case will not be proceeding by mid-February. The Plaintiffs' pleadings have already been amended to put their case on a sounder footing and there is a chance that they will amend their pleadings yet again to include an allegation of loss flowing from anti-trust breaches

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in 1980/81 to pick up the price fixing breaches we understand the DOJ Grand Jury was investigating (which the terms of the DOJ's pronouncments after the US Government's decision may well serve to encourage).

8. There can be no guarantee that even if the liquidator's action is settled the class actions will disappear. The chances of this do not now appear favourable, particularly if the separate 1980/81 breaches are pleaded (although it is possible that the damages from these breaches alone may be relatively as small as 30 million US dollars). BA's US lawyers consider that they could win the class action as currently constituted on points of law, but these are novel points and here also they can give no assurance. The likelihood is that by mid-February this class action will still be hanging over BA and the appropriate assessment will have to be made at the time and disclosed in the prospectus.

9. An agreement with the US Government over future arrangements taking UK airlines out of US anti-trust law (provided the requirements of transparency are met) will not solve the above disclosure problems because there can be no expectation that that agreement will apply to affect civil suits already commenced.

10. We have reason to believe that there are other possible grounds for potential liability outside the immediate Laker issues. If class action plaintiffs fish in the right waters (as they are permitted to do under US law) they may discover the scheduling agreements in breach of US anti-trust of which the DOJ is believed to have found evidence, which could also form the grounds for a new treble damages claim. The danger is that unless there is a global settlement (or at least one involving B Cal as well as BA) of the liquidator's suit further disclosures in that action could lead to re-constituted, or fresh, class actions, feeding upon any new breaches of anti-trust which have been disclosed. We are told

/that

that the DOJ may be interested in pursuing its suspicion that TWA and Pan Am have been guilty of perjury and obstruction of justice in relation to their anti-trust liability. If the DOJ gets anywhere with that, it is not inconceivable that BA could be brought back into the arena of non-Laker related criminal anti-trust indictments (which in turn could spark off further civil actions.) 7

11. It is not known whether BA has other incriminating documents in the USA disclosing other anti-trust breaches. In the light of the existing state of affairs discussed above, it is not thought safe that this possibility can be ignored. A full investigation is being undertaken. If any incriminating documents are found advice will have to be taken on whether they can properly under US law be destroyed. An agreement with the US Government may assist in the area of other potential civil liabilities but we cannot guarantee that it will and at the moment it does not appear likely.

ANNEX B

BRITISH AIRWAYS FLOTATION: KEY DATES

3-7 DECEMBER 1984:	INVITATIONS ISSUED TO INSTITUTIONS
7 JANUARY 1985 :	MARKETING SEMINARS BEGIN
22 JANUARY 1985 :	PATHFINDER PROSPECTUS ISSUED
14 FEBRUARY 1985:	IMPACT DAY, SALE PROSPECTUS PUBLISHED

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ANNEX C

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DRAFT: PWRWG/~~28.11.84~~

PRIVATE AND CONFIDENTIAL

* Under United States practice this might permit the Court to impose sanctions that could prejudice the defence of the case.

On 24 November 1982 the Liquidator of Laker Airways Limited brought legal proceedings in the United States District Court for the District of Columbia against certain trans-atlantic airlines and other companies, including British Airways, claiming violations of US Federal Anti-Trust laws, in that they had conspired to drive Laker out of business and, in tort, that they had intentionally caused injury to Laker. The complaint seeks treble damages and penalties in excess of $1bn. British Airways has answered denying all material allegations and asserting various affirmative defences. The case is in the stage of pre-trial discovery. The company's ability to comply with certain discovery requests directed to it in accordance with United States procedures has been limited by blocking orders entered by the Secretary of State for Trade and Industry under the United Kingdom Protection of Trading Interests Act 1980.* Both management and Paul, Weiss, Rifkind, Wharton and Garrison, US trial counsel to British Airways, believe, after investigation, that the evidence of which they are aware does not support a reasonable conclusion that British Airways engaged in the alleged conspiracy to drive Laker out of business or that British Airways tortiously or unlawfully caused any injury to Laker.

However, No assurance can be given that Laker will not be able to submit its claims for decision by a jury; nor can any assurance be given as to the jury's verdict or the impact of the blocking orders.

British Airways, Pan American and TWA are also defendants in a consolidated anti-trust class action filed on 21 November 1984 in the same United States District Court, which claims unquantified damages and penalties on behalf of trans-atlantic air passengers following Laker's cessation of business in February 1982. The consolidated complaint alleges that the defendants conspired to fix prices for certain categories of fares for US/UK air travel, causing members of the class to pay higher prices for such air travel during the period from 1 March 1982 to at least 3 December 1983.

The same
Trial counsel believe there are substantial legal and factual defences to this action, including a statutory exemption from anti-trust liability provided under US law. While this action raises novel legal questions trial counsel believe the defences should prevail, but the outcome cannot be predicted with certainty.

While the Directors cannot be sure that the financial position of the company will not be adversely affected, they have concluded, on the basis of present information and ~~the foregoing,~~ its legal advice, and having regard to the many factors which affect this type of litigation in the United States, that [redacted] it is not appropriate to make any provision.

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File

File
– BA Privat.

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SECRET

MR REDWOOD

30 November 1984

BA PRIVATISATION

The story is not a happy one. The successful launch of BA before the end of the current financial year is no longer achievable.

The principal obstacle is the Laker anti-trust cases, but I suspect that, even with that removed, the time required to resolve the capital structure question would jeopardise the timetable.

In calling off the Grand Jury investigation into the allegations of anti-trust action by various airlines against Laker, Reagan removed one threat to BA's future liabilities. There are two others. The Laker liquidator is pitching for damages claimed to approach $1 billion. Opportunistic US lawyers are pursuing class actions (nominally on behalf of passengers denied competitive Anglo-US air fares) which could entail additional claims again approaching $1 billion.

Faced with the need to address the question of Laker-related liabilities in the privatisation prospectus, BA initially produced a bland draft to the effect that the claims were not felt to have a substantial legal basis. Transport and their lawyers were nervous, and insisted that they needed to test BA's position. It emerges that BA have never conducted their affairs with a view to protecting themselves against anti-trust allegations. They are, therefore, sitting on documentary evidence which makes it far from certain that they are invulnerable. Now, BA, their lawyers, Transport and their lawyers, all accept that any honest statement that they could make about Laker-related liabilities would effectively make the prospectus unsaleable.

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Four options have been considered to salvage the February 1985 launch of BA:

1. Quickly settle out of court with the Laker liquidator.

Preliminary negotiations have taken place, so this could be quickly picked up. BA would have to offer £10-20 million and, up against time pressure, could easily end up settling for more. The other airlines being pursued by the Laker liquidator, including BCal, would claim that BA had sold the pass because of the Government's bull-headed pursuit of privatisation. BCal might be inclined to make a legal claim against BA on the grounds that their commercial interests were subordinated to the Government's privatisation objectives.

In view of this, Transport are adamant that any quick settlement with the liquidator would have to include BCal. Because of the sums of money, BCal won't want to be pressured into a quick, expensive settlement.

In any case, dealing with the liquidator would only half close the door. The class actions would remain, perhaps stimulated by the scent of blood if BA are seen to scramble for a quick settlement. (Class action claims can be upped as each new piece of evidence comes to light.) The prospectus would still have to confront this liability.

In all, option 1 is seen as a blind alley.

2. The Government undertakes to indemnify BA against Laker-related claims.

In effect the Government would be writing a blank cheque drawn on the taxpayer. It would stiffen the resolve of the

liquidator and the class action lawyers, whilst removing from BA the responsibility to defend themselves vigorously.

No go.

3. BA maintain that it would be possible to insure themselves against future Laker-related liabilities.

Any insurer faced with a realistic appreciation of BA's situation (and they would insist on getting all the facts) would have to charge a very high premium, even assuming that they were prepared to take on the liability.

No go.

4. The Government toughs it out with the US Government insisting that it is outrageous for BA to be put in this situation, particularly bearing in mind Bermuda 2.

Ridley instinctively favours this option, but it would not further the cause of BA privatisation. This scenario could entail unpleasant side effects (seizures of BA aircraft by the US and vice versa) with a lot of political downside.

Given that the BA privatisation timetable is a lost cause, we still have problems. It is well known in the City and Fleet Street that the button is about to be pressed for the BA launch. Transport think that they can find a pretext other than Laker for the postponement. They must be naive. Once it is known that BA and the Government are running scared on Laker, the US lawyers will see the stakes as being raised.

By comparison, yesterday's intended wrap-up meeting on the capital structure of BA post-privatisation was a sideshow. Nothing was resolved. BA bid for a £400 million injection of equity from the Government. Hill Samuel

(representing HMG) maintain that BA need at least 70:30 equity/debt a few months after privatisation. They translate this into the requirement for a £350 million equity injection. Accepting 70:30, but using their own expenditure and profit forecasts, Transport estimate that £250 million should be sufficient. Treasury want to stand firm on £150 million. Ridley, even more hawkishly, insisted at yesterday's meeting that BA should go away and consider £100 million. The match continues, and will not be resolved until the very end.

JOHN WYBREW

SECRET

FCO 84

2

10 DOWNING STREET

From the Private Secretary

27 November, 1984

UK/US: Discussions on Civil Aviation

I enclose a copy of a message to the Prime Minister from President Reagan received in No. 10 this afternoon. As you will see, it is relevant to your Secretary of State's meeting with Mr. Dam tomorrow morning. I should be grateful for a draft reply in due course, but suggest that this should follow the discussions and take account of the results.

I am copying this letter and enclosure to Colin Budd (Foreign and Commonwealth Office), Callum McCarthy (Department of Trade and Industry), David Peretz (Treasury) and Henry Steel (Law Officers' Department).

C. D. POWELL

Miss Dinah Nichols,
Department of Transport

SECRET

(2)

Prime Minister
Copies passed to
Sir G. Howe &
Mr. Ridley
CDJ
27/XI

SECRET

Dear Margaret:

I agree wholeheartedly with the observation in your November 19 letter that we must make every effort to resolve some of the outstanding differences in the civil aviation field. Reflecting the great importance which I attach to these discussions, I have asked Deputy Secretary of State Kenneth Dam to initiate this process. He is scheduled to meet with Sir Geoffrey Howe and Mr. Nicholas Ridley on Wednesday, November 28, and I hope that he and your ministers will be able to make significant headway in this essential area. As Under Secretary Allen Wallis mentioned to you on November 18, we believe this should include:

(1) substantial pricing flexibility;
(2) a relaxation of capacity restrictions;
(3) full disclosure of price coordination talks;
(4) Her Majesty's Government's commitment not to invoke its blocking statute against U.S. enforcement actions against violations and to stress to carriers the need to comply with U.S. antitrust laws.

I sincerely believe that progress in these areas will be in the best interest of both our countries.

Nancy and I are looking forward to seeing you next month.

Sincerely,

//S//

Ron

SECRET

EMBASSY OF THE UNITED STATES OF AMERICA
LONDON

November 27, 1984

Dear Prime Minister:

I have been asked to deliver the attached message to you from President Reagan, which was received at the Embassy early this morning.

Sincerely,

Charles H. Price II
Ambassador

Enclosure:

SECRET

The Rt. Hon. Margaret Thatcher, M.P.,
Prime Minister,
10 Downing Street,
London S.W.1.

Aerospace: CAA Review: PE3

Subject Mark

SECRET

Dear Margaret:

I agree wholeheartedly with the observation in your November 19 letter that we must make every effort to resolve some of the outstanding differences in the civil aviation field. Reflecting the great importance which I attach to these discussions, I have asked Deputy Secretary of State Kenneth Dam to initiate this process. He is scheduled to meet with Sir Geoffrey Howe and Mr. Nicholas Ridley on Wednesday, November 28, and I hope that he and your ministers will be able to make significant headway in this essential area. As Under Secretary Allen Wallis mentioned to you on November 18, we believe this should include:

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(2) a relaxation of capacity restrictions;
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I sincerely believe that progress in these areas will be in the best interest of both our countries.

Nancy and I are looking forward to seeing you next month.

Sincerely,

//S//

Ron

SECRET

22/252

CONFIDENTIAL

Treasury Chambers, Parliament Street, SW1P 3AG

Rt Hon Nicholas Ridley
Secretary of State for Transport
Department of Transport
2 Marsham Street
LONDON
SW1P 3EB

8 November 1984

Dear Nicholas,

CIVIL AVIATION BILL: LIMIT ON AIR TRANSPORT MOVEMENTS

Thank you for your letter of 8 November.

It is of course most inconvenient to all of us that British Airways made their claim about the effect on them of the ATM limit just as Legislation Committee was about to consider your proposed Bill. But given that the claim had been made it seemed to me and to the Economic Secretary that it should be investigated before the Bill could be introduced. On the face of it the claim completely altered the financial implications of the policy which E(DL) had considered in April. I am sorry that this came as a surprise to you: I understood that your officials were aware of BA's claims certainly no later than officials here.

I agree entirely with your assessment of BA's motives in putting forward their forecasts of capital expenditure. Had they done so before E(DL) had considered your proposals there would have been an opportunity for their claims to be scrutinised; and for some assessment to be made of the financial consequences.

I am delighted to see that you do not accept that the ATM legislation in any way weakens your negotiating position with BA over their capital structure. It must obviously be your aim in the negotiations to point out to BA the weakness of their argument. In particular you will need to persuade BA of the force of your contention that they have open to them options for living within the ATM limit which do not involve substantial capital investment. I hope that your officials

will pursue that argument vigorously with BA. It should be capable of quantification in discussion with BA. I should be grateful if my officials could be involved in this.

On the understanding then, that although your officials will be taking up these points with BA you see no need to provide for any impact of the ATM limit in BA's capital structure I would be content for the Civil Aviation Bill to be introduced today.

I am sending copies of this letter to the recipients of yours.

JOHN MOORE

CONFIDENTIAL

cc NO

NBPM AT 8/4

010

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

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

8 November 1984

Dear Chancellor,

CIVIL AVIATION BILL: LIMIT ON AIR TRANSPORT MOVEMENTS

As you know, I planned to introduce a Civil Aviation Bill this week. I was surprised and dismayed to learn that at 'L' Committee yesterday the Economic Secretary objected to the Bill on the grounds that it might have substantial public expenditure implications, although E(DL) had already given policy approval. He based his arguments on British Airways very recent projections of future capital expenditure (on aircraft), which they claim they would be bound to incur by adhering to the projected limitation of air traffic movements (ATMs) at Heathrow to 275,000 per annum.

British Airways have two motives in putting forward their capital expenditure forecasts, (which are higher than anything that they have previously suggested):

(a) to persuade the Government that they will need a substantial capital injection at privatisation (Lord King has suggested £400m);

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(b) to forestall the imposition of the ATM limit, which they oppose (by suggesting that it would involve them in a great deal of expenditure on larger aircraft, to cater for traffic growth without increasing ATMs).

I do not accept BA's figures, and I intend to challenge the Board on them. But I cannot do this until I have counter-proposals to put to them on their capital structure after discussion with you and my advisers.

BA have founded their forecasts of capital expenditure on a fleet plan which they acknowledge themselves assumes growth in the market and which "primarily aims to provide capacity in a form best suited to market requirements." They have also taken account of the constraints which they perceive will be imposed by the ATM limit. However, I do not believe that BA's projected expenditure is made necessary entirely, or even mainly, by the ATM limit (although, as I have indicated, it is clearly in BA's interest to give us this impression and I cannot expect to get out of them any dependable information on the precise effect of this factor alone).

I must impress upon you that there is no direct connection between BA's capital expenditure projections and the Civil Aviation Bill. Even with the ATM limit there will be no compulsion on BA to make the capital investment they now claim they want to make: they will still have the option of not making it and, if these present figures are correct, of carrying only as much traffic as they can with the equipment they have. This might lead them to lose market share and will also affect their competitors at Heathrow; but it will not, on their present figures, lead to an appreciable loss of profitability or therefore damage the prospects for the privatisation or for the proceeds. But, on the pattern of the past, I rather suspect BA will find, once the argument is ended, that they can in any case make do with less investment than they now allege.

I do not like the ATM limit any more than you do; but, as you know, it is a declared Government commitment and I have to make provision for its effective introduction next year. If I were to let it be known that the 275,000 limit was not after all to be imposed, we might find ourselves having to reopen the Stansted/Terminal 5 inquiry (during which we reaffirmed that the limit would be imposed). As I have always made clear, after I have had experience of the limit's operation I am ready to review it and, if there is a sound case, relax it.

In the light of my remarks I hope that you will see the importance of divorcing the two issues of BA's capital structure and the ATM legislation. I do not accept - or intend - that the Bill will in any way weaken my position in the forthcoming negotiations with BA over their capital structure. On this basis may I have your agreement without more delay to the introduction of the Civil Aviation Bill?

Unless I can have your agreement to this this morning, I must seek an immediate meeting with you. The Business Managers indicated at 'L' Committee yesterday that in order to meet the necessary deadline for Royal Assent the Bill will need to be introduced today and published on Friday.

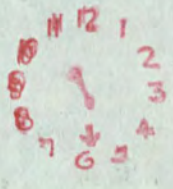
I am copying this letter to the Prime Minister, Patrick Jenkin, members of 'L' Committee and Sir Robert Armstrong.

Yours sincerely,

Nicholas Ridley

pp NICHOLAS RIDLEY

(approved by the Secretary of State & signed in his absence)



Ref. A084/2642

PRIME MINISTER

Airline Competition Policy
(C(84) 27)

BACKGROUND

The Civil Aviation Authority (CAA) was invited by the Secretary of State for Transport to review the implications of the privatisation of British Airways (BA) for competition and the A sound development of the British airline industry. The report of the CAA in response to that invitation was published on 16 July. Among its main recommendations were the following:

(i) Relinquishment by BA of scheduled service routes out of Manchester and Birmingham to a wide variety of destinations in Western Europe; between Glasgow and Paris; between Heathrow and Saudi Arabia and between Heathrow and Harare; and between Gatwick and points in Spain, Portugal, Gibraltar, Italy and Scandinavia. Apart from the Manchester and Birmingham routes, which would pass to smaller airlines, the routes concerned would be likely to be awarded by the CAA to British Caledonian (BCal).

(ii) A number of measures to increase competition in the British airline industry.

(iii) A strengthening of the CAA's own powers, notably to give the CAA a direct statutory duty to secure the sound development of the British airline industry, for example by suitable use of its licensing powers.

2. Ministers collectively have considered the recommendations B. on several occasions, both in E(A) (E(A)(84) 19th Meeting, Item 3) and in Cabinet (CC(84) 27th, 28th and 29th Conclusions). It has been common ground that the recommendations summarised at (ii) above should be accepted and those at (iii) rejected. There has, however, been a sharp difference of view on the recommendations

concerning route transfers. At their meeting on 2 August (CC(84) 29th Conclusions, Minute 5) the Cabinet invited the Secretary of State for Transport to prepare a further paper discussing the issues. You said that you would arrange for a small Group of Ministers under your chairmanship to give preliminary consideration to those issues before the Cabinet resumed their discussion.

3. At the beginning of September, the Secretary of State for Transport circulated a paper to the Cabinet (C(84) 22) discussing a number of possible route transfers from BA to BCal and suggesting that if, as seemed likely, they were not acceptable to Lord King and his Board, it would be necessary to promote primary legislation in the new Session of Parliament to achieve them.

4. The proposals in C(84) 22 were not discussed by the Cabinet. Instead, they were considered by a small Group of Ministers at a meeting under your chairmanship on 11 September. The main conclusions of that meeting are summarised in paragraph 3 of Mr Ridley's current memorandum (C(84) 27). In particular, the meeting agreed thatit would not be feasible to legislate; and that the right approach was therefore to try to persuade BA and BCal to agree to a negotiated "route swap".

5. C(84) 27 puts forward proposals on the basis of Mr Ridley's negotiations with BA and BCal. He proposes that BA should give up its routes to Saudi Arabia in return for the route to Atlanta in the Southern United States, and a number of other routes, mainly to Latin America. Details are given in Annex B to C(84) 27.

6. Neither BA nor BCal has given a definitive statement of its views. Discussions are still in progress; but I understand that the situation is as follows:

(a) BCal has said that it would accept the package in C(84) 27 if it could keep the Atlanta route: it has not said that it would reject the package if it could not keep that route, but the Department of Transport consider that it might well do so.

(b) BA has said that it would accept the package as it stands; the Department of Transport assessment is that it would probably not accept if it did not obtain the Atlanta route.

7. The proposed deal would, according to BA, reduce their profits by £17 million a year and increase BCal's by £15 million a year. Mr Ridley suggests that it might reduce the proceeds from floating BA by £80-£100 million.

8. C(84) 27 also contains proposals on the other CAA recommendations, as follows:

(i) The CAA's recommendations on domestic air services and dual designation on those overseas routes where dual designation is possible should be accepted (paragraphs 5 and 6 of the memorandum).

(ii) Instead of transferring BA's European routes out of provincial airports to other British airlines, Mr Ridley proposes to accept an offer from BA of limited financial and other support for airlines wishing to set up on such routes (paragraphs 7 and 8 of the memorandum).

(iii) Stronger action, on the lines described in paragraph 13 of the memorandum, should be taken against predatory pricing and other anti-competitive behaviour.

(iv) The CAA's request for wider licensing powers should be rejected.

(v) Nothing can be done about increasing capacity at Heathrow and Gatwick for the time being (paragraph 14ii. of the memorandum).

9. Mr Ridley proposes that the Government's conclusions should be made known in a White Paper to be published forthwith: the aim would be to make the Government's decisions public before the Party Conference.

MAIN ISSUES

10. The main issues before the Cabinet are as follows:

(i) Is the proposed deal between BA and BCal satisfactory?

(ii) If it is not, what prospects are there of obtaining a better one:

(a) by legislation; or

(b) by other means?

(iii) Are Mr Ridley's other proposals acceptable?

(iv) How should the Government's decisions be announced?

In practice, questions (i) and (ii) cannot be divorced: there is no point discussing what might be ideal arrangements if there is no way of bringing them about.

Is the deal satisfactory?

11. The following main considerations seem relevant:

(a) The effects on competition. Clearly it would be desirable to have two, or more, strong British airlines freely competing on all international routes. Unfortunately, because competition in air transport is so heavily restricted by international agreements, it is not a possibility for the foreseeable future. The CAA's proposals are rather directed at strengthening the financial position of BCal by allowing it to enjoy monopoly-type profits on some routes, so that it can compete more effectively on others. Is this a valid approach? If it is, do Mr Ridley's proposals go far enough in that direction?

(b) The implications for privatisation. Hill Samuel, the merchant bankers advising the Government on the BA flotation, suggested earlier that any package of route transfers which reduced BA's profits by more than 10 per cent would carry an unacceptable risk to privatisation. BA estimate that the effect of Mr Ridley's proposals would be to reduce their profits by £17 million a year (about 6 per cent). Presumably this would not be a bar to privatisation. Nevertheless, it would entail a reduction in the proceeds of sale and probably, for the reasons outlined in paragraph 10ii. and iii. of the memorandum, in the amount received by the Government.

(c) The public attitude of the airlines. If BA and BCal will at least acquiesce in the deal, Ministers are likely to regard it as a satisfactory solution to a very difficult problem. But it is not clear that BCal, in particular, will. If they reject the deal, it is not clear that the defence outlined at the end of paragraph 12 of C(84) 27 will carry conviction in public debate. The deal which BCal would have rejected is much less favourable to the airline than the CAA's recommendations. The Government will presumably, at the very least, have to produce convincing reasons why it has departed from those recommendations.

12. It seems quite likely that, when the Cabinet take their decisions tomorrow, the positions of BA and BCal regarding either the proposed deal or possible modifications to it will not be known with certainty. If so, Ministers will need to decide on their response should either or both airlines reject the deal. Should they, in effect, say that the proposals were the Government's last word, and that if they are rejected that is an end of the matter; or do they wish to invite the Secretary of State for Transport to try to find an alternative?

Could a different deal be obtained?

13. If, for whatever reason, the Cabinet thought it desirable to try to secure different arrangements to those proposed in C(84) 27, it would be necessary to consider the means by which this might be done. The possibilities are as follows:

(a) Legislation. This would be highly contentious and delay privatisation. Moreover, the business managers have advised that the passage of legislation could not be guaranteed. The meeting on 11 September decided that these were conclusive objections.

(b) Amending BA's Articles of Association. There are legal difficulties about this course; it might well cause the Board of BA to resign; and there are objections of propriety to reducing the value of substantial public assets otherwise

than by legislation. In his earlier memorandum (C(84) 22) Mr Ridley regarded these objections as conclusive; and that view has not been challenged.

(c) Further negotiations. Mr Ridley argues in paragraph 12 of his memorandum that further negotiation would serve no useful purpose. The Cabinet may wish to probe this. The Atlanta route is no doubt important to BCal. Are there other routes to America or elsewhere which might be less valuable to BCal but still attractive to BA? Does the contract for trooping flights to the Falklands (Mr Ridley's letter of 2 October to Mr Heseltine) offer a possible solution?

Other proposals

14. If, as seems likely, the Cabinet rule out the possibility of legislation, then there seems to be little alternative to accepting BA's offer on European routes from provincial airports. It seems unlikely that any Minister will challenge Mr Ridley's recommendations on domestic air services; dual designation; action against anti-competitive behaviour; CAA licensing powers; or traffic movements at Heathrow and Gatwick.

Announcements

15. There is no formal need to announce the Government's decisions by a White Paper: if Parliament were sitting a written or oral statement would probably suffice. But Parliament is, of course, in Recess; and Mr Ridley considers that a Press Notice would not be enough.

16. If the proposed deal is accepted by BA and BCal, then the draft White Paper attached to C(84) 27 seems broadly satisfactory. But if the deal is not accepted, Ministers will wish to consider whether a more aggressive justification than that recommended by Mr Ridley in paragraph 12 of C(84) 27 is needed. In previous discussions, some Ministers have argued that it would be necessary in such circumstances to argue publicly that the CAA's recommendations would not in fact promote competition and would indeed weaken BA, the main United Kingdom flag carrier, as a competitor to overseas airlines. If the Cabinet should decide to

adopt this approach, fairly substantial recasting of the draft White Paper will probably be needed. In such circumstances, you will probably wish to invite Mr Ridley to circulate a revised draft to the Cabinet, with sufficient time for Ministers to give it full consideration.

17. The timing of the announcement also requires consideration. Mr Ridley has proposed immediate publication of the White Paper, no doubt because it was felt that an announcement before the Party Conference would be desirable. But much will depend on what further progress Mr Ridley is able to report, on whether the Cabinet considers that further negotiations might be worth while and on how much extra work needs to be done on the draft White Paper. If no announcement is possible before the Party Conference, there will need to be agreement on a form of words to hold the position - for example that further discussions are taking place.

HANDLING

18. You will wish to invite the Secretary of State for Transport to open the discussion. The Chancellor of the Exchequer will wish to comment on the implications for competition and for the privatisation programme. The Secretary of State for Trade and Industry will also wish to comment on the implications for competition. The Lord Privy Seal and the Chief Whip can advise on the Parliamentary aspects.

CONCLUSIONS

19. You will wish the Cabinet to reach conclusions on the following:

(i) Are the proposals in C(84) 27 for route transfers between BA and BCal satisfactory?

(ii) If not, how should attempts be made to amend them?

(iii) If they are rejected by either BA or BCal, what should be the Government's response?

(iv) Are the proposals in C(84) 27 on:

(a) domestic air services;

(b) dual designation;

(c) European services from regional airports;

(d) action against anti-competitive behaviour;

(e) CAA licensing powers;

(f) air traffic movements from Heathrow and Gatwick

acceptable?

(v) How and when should the Government's decisions be announced?

Approved by
ROBERT ARMSTRONG
and signed in his absence

3 October 1984

CONFIDENTIAL

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

Richard Hatfield Esq
Private Secretary to
Sir Robert Armstrong GCB, CVO
Secretary of the Cabinet
Cabinet Office
70 Whitehall
LONDON SW1A 2AS

3rd October 1984

Dear Richard,

AIRLINE COMPETITION POLICY

My Secretary of State's paper on Airline Competition Policy (C(84)27), which is on the agenda for tomorrow's Cabinet, covered a draft White Paper on aviation policy. Paragraph 12 of the covering paper explained that the withdrawal of British Caledonian from Atlanta remains a sticking point in the negotiations on route exchanges; and my Secretary of State will be reporting orally to Cabinet the case put by both British Airways and British Caledonian concerning Atlanta in discussions he has held with both airlines since the paper was circulated.

He felt however that colleagues would wish to see an alternative draft of the White Paper, should the proposed route exchanges not be accepted by British Caledonian. The attached two paragraphs would replace the section from the square bracketed last sentence of paragraph 22 to the end of paragraph 25 of the draft White Paper. In addition, the bracketed sentences in paragraph 15 and at the end of paragraph 18 would be deleted.

I am copying this letter to the Private Secretaries to the members of Cabinet.

Yours,

Diana

MISS D A NICHOLS
Private Secretary

CONFIDENTIAL

AVIATION POLICY WHITE PAPER

ALTERNATIVE DRAFT TO END PARAGRAPH 22 TO PARAGRAPH 25

A Instead of compulsory transfers, the Government favoured a reciprocal arrangement to strengthen British Caledonian financially, under which each airline would have withdrawn from routes which the other might then have taken up. The Government has explored this possibility with the two airlines. It persuaded British Airways to put forward proposals for an exchange of routes which would have increased British Caledonian's pre-tax annual profits by about £15m without substantially reducing the scale of British Airways' activity. The Government believes this exchange would have been to British Caledonian's advantage and would have enhanced its ability to compete with both British Airways and foreign airlines. Unfortunately British Caledonian has not felt able to accept the exchange.

B The Government regrets this outcome. It means British Caledonian will be less well placed than it could have been to exploit early opportunities for dual designation. But in the Government's view, given its record of past achievements and its improving profitability, British Caledonian should still be able to take advantage of such opportunities, perhaps at a more moderate pace than might otherwise have been the case.

CONFIDENTIAL & COMMERCIAL IN CONFIDENCE

a ~~AJ~~

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

The Rt Hon Michael Heseltine MP
Secretary of State for Defence
Ministry of Defence
Main Building
Whitehall
LONDON SW1A 2HB

2 October 1984

Dear Michael

CAA REVIEW OF CIVIL AIR TRANSPORT

I have circulated a paper to Cabinet about the response we should make to the Civil Aviation Authority's proposals, and we shall be discussing that on Thursday. However the signs are that it will be extremely difficult to secure agreement of British Airways and British Caledonian to the route exchange which I have suggested in the paper. The difficulty is the transfer of BCal's route to Atlanta. BCal regard it as too high a price to pay, while British Airways have so far refused to agree to the deal without the inclusion of Atlanta.

Lord King has however indicated to me that he might find that possible if he could find some other way of using the resources (aircraft and crew) which would have been transferred to it from routes given up by British Airways. This would be possible if he secured the contract for trooping flights to the Falkland Islands for which British Airways were recently invited to tender by your Department. I understand that the bids received from the tenderers

are still being evaluated by your Department, and I am writing to urge you to accept the British Airways' bid, if it is the best, and help clear the way to a solution of the problem which has been raised for the Government by the CAA's route transfer proposals.

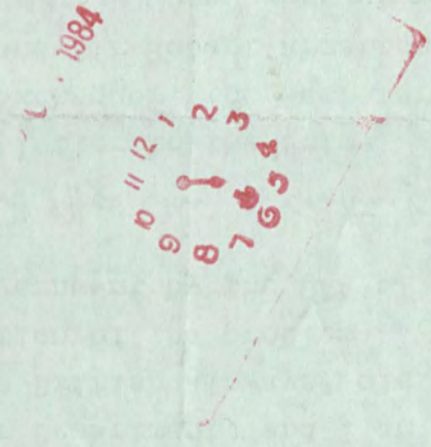
Is it possible that you could offer, say, a contract for 3 years?

I am sending copies of this letter to the Prime Minister, the Chancellor of the Exchequer, the Secretary of State for Trade and Industry and Sir Robert Armstrong. I should be grateful if you could let me know very quickly what you can do.

Yours ever

Nicholas

NICHOLAS RIDLEY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PART 2 ends:-

Lord King (British Airways)
to SS/Transport 27.9.84

PART 3 begins:-

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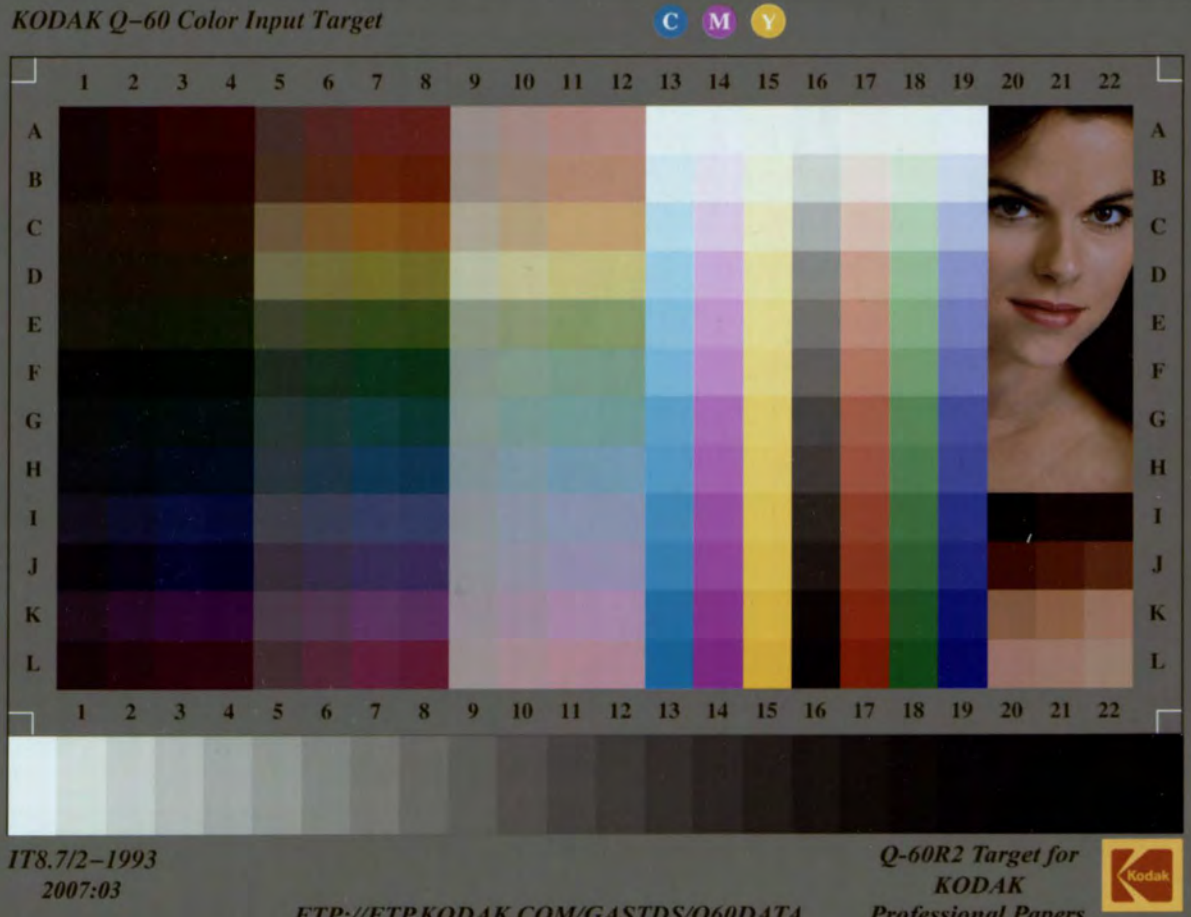
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