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PREM 19/2200

Confidential Filing

The Secretary of State for Defence wished to set up a working group to examine whether the Atomic Weapons Research Establishment, Aldermaston (three) should remain under the control of the Ministry of Defence and the implications for the nuclear Royal Ordnance factories.

GOVERNMENT
MACHINERY

September 1980

Referred to	Date	Referred to	Date	Referred to	Date	Referred to	Date
22.9.80		25.3.82					
8.10.80		18.5.82					
15.10.80		22.7.88					
31.10.80							
16.2.81							
26.2.81							
12.6.81							
18.6.81							
19.6.81							
23.6.81							
30.6.81							
7.7.81							
1.7.81							
13.7.81							
17.7.81							
28.7.81							
15.2.82							

PREM 19/2200

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Treasury Chambers, Parliament Street, SW1P 3AG

The Lord Trefgarne
 Minister of State for Defence Procurement
 Ministry of Defence
 Main Building
 Whitehall
 London
 SW1A 2HB

celo
 CDP
 27/7.

26th July 1988

Dear David,

**BRITISH AEROSPACE: LONG TERM AMMUNITION SUPPLY
 AGREEMENT WITH ROYAL ORDNANCE PLC**

Thank you for your letter of 22 July.

I agree that this announcement should be made. It is consistent with the earlier commitment given by George Younger at the time of the sale of ROplc to BAe, and the figures negotiated are better than the payments that would be made under the existing agreement. I note the likelihood of controversy in the light of the sale of Rover to BAe, and of accusations that we are restricting competition. Nonetheless, as you point out, other UK suppliers will not be prohibited from competing for a reasonable proportion of the market. Therefore, such an agreement can only represent long term value for money in defence procurement.

I am sending copies of this letter to the Prime Minister, David Young, Malcolm Rifkind and Peter Walker.

Yours Ever,
John

JOHN MAJOR

Govt Mach: Control
of Royal Ordnance Fact
Sept 80



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Minister of State
for Defence Procurement

D/MIN(DP)/DGT/5/3/1/1/1

MINISTRY OF DEFENCE
WHITEHALL LONDON SW1A 2HB

Telephone 01-218 6621 (Direct Dialling)
01-218 9000 (Switchboard)

22 July 1988

Ric Austin

You should be
aware of this, which
could be criticised

Dear John,

BRITISH AEROSPACE: LONG TERM AMMUNITION SUPPLY AGREEMENT
WITH ROYAL ORDNANCE plc

C80
22/7.

When we sold Royal Ordnance plc to BAe in April last year after failing to float the company, George Younger told the House that a feature of the agreement was an undertaking to enter into discussion on a long term contract for the supply by RO to the Ministry of Defence of explosives, propellants and ammunition. This undertaking was embodied in Heads of Agreement signed between the MOD and BAe which envisaged that RO would supply 80% of the Ministry's requirements for these items (broadly speaking our conventional ammunition needs) over a five year period from 1st April 1988 at fixed and annually reducing prices. Failing Agreement by March of this year the Heads provided for the continuation until March 1991 of a current but more limited agreement giving RO exclusive rights to supply explosives and propellants, but not the ammunition natures they fill. The Heads also provided for negotiation for the wider five year agreement to continue past March 1988.

Both our current explosive and propellant (E and P) agreement and the wider five year agreement embracing ammunition

/ owe ...

The Rt Hon John Major MP

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owe their origin to the desire to move RO into the private sector. RO have an over-large and uneconomic production base for ammunition which needs extensive rationalisation. Both our advisers prior to the intended float and the prospective purchasers of the company recognised the problem. Hence both the current E and P agreement and the Heads of Agreement reflect the perceived need for a degree of protection for RO while it rationalises its production base and makes itself competitive in international markets.

There are differences of view between ourselves and BAe over the extent to which we are committed under the Heads of Agreement to the five year arrangement or are free to fall back on the more limited E and P procurement route. Our own legal advice is that we are free to do so, but the matter is not wholly free from doubt. I have nevertheless made it clear to BAe throughout that prices offered would be crucial and would need to be sufficiently attractive to persuade us to the merits of the five year agreement.

After some protracted and tough negotiations we have now reached the position where we have a final BAe/RO offer of some £396m under the five year arrangement. As well as standing up to our Technical Costs scrutiny, this shows an advantage of some £35m (8.5%) over the only other course open to us (assuming we are right in our interpretation of the Heads of Agreement) which is to extend the E and P agreement for three years. In making the financial appraisal underpinning this assessment we have taken account of competitive offers from alternative domestic as well as other NATO suppliers. A five year contract with RO has added practical advantage in assurance of supply nationally and well

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established quality standards which are obviously important in relation to dangerous materials of this kind. Judged from a wider perspective the RO prices indicate that, by the end of the five year period, the company should indeed have slimmed down and rationalised its operations and, as intended, have become competitive on world markets.

Also included in the Heads was provision for a one-time lump sum payment by the MOD of £12m towards RO's defined and incurred rationalisation costs. This has been negotiated down to £10m and, rather than a lump sum, will be subsumed in the prices of ammunition purchased during the first year of operation of the agreement. Overall this gives a total contract price of £406m.

I am satisfied, therefore, that the prices now offered to the MOD represent good value for money and intend to announce on Thursday, 26th July, that the Ministry will shortly be placing a five year order for 80% of our conventional ammunition requirement with RO.

You and colleagues will wish to be aware that award of these orders will be controversial. There has been substantial Parliamentary interest in the outcome of the negotiations both among the 50 or so Members with RO constituency interests and those other colleagues who see any five year arrangement of this scale with RO as damaging to the Government's competition policies and to the prospects of other, smaller, firms anxious to expand operations in the UK domestic ammunition market such as Astra-BMARC and Pains Wessex. In addition, the recent problems encountered over the sale of Rover to BAe may lead to our proposed

/ arrangement ...

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arrangement with RO being presented as a "back door" subsidy to the Group.

There is indeed a measure of conflict between what were necessary steps to secure the successful move of RO into the private sector and the limitations they will impose in the short term on freedom of competition in this sector of the market, but this needs to be kept in proportion. RO is the predominant national supplier of explosives and ammunition, and until January 1985 was the approved preferred source for almost all our requirements. Potential domestic competitors accordingly cannot currently offer an equivalent range of capabilities. The annual value of the items to be covered in the five year agreement varies between about £100m in 1988/89 down to some £60m in 1992/93. Our best estimate is that there will still be some £35m of work available in the first year alone to be placed with other suppliers plus whatever element of the RO work the company itself chooses to sub-contract (in the region of 25% last year). There remains, therefore, a reasonable proportion of our work open to competition relative to the capacity of others in the industry, although I must point out that RO will itself be free to bid for a part of this work.

There are conflicting pressures here, but looked at in terms of value for money, I believe we have now received sufficiently attractive prices to be readily defensible against attacks on the apparent curtailment of competitive opportunities over the period of the agreement. We should also achieve, as envisaged in privatising RO, an overdue and much needed rationalisation of our major domestic producer which will enable it to compete much

/ more ...

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more successfully in world markets.

I am sending copies of this letter to the Prime Minister,
David Young, Malcolm Rifkind and Peter Walker.

Yours,
David

Lord Trefgarne

It may be better to announce
on Wednesday to avoid the
charge of trying to "muggle"
this out on the last day.
D.

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✓ BS
MAP

MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1
Telephone 01-~~938 7022~~ 218 6169

MO 10/4

18th May 1982

PA

Told Mr Piper PM wd almost
certainly not see; and that they
shd go ahead if other Ministers
agreed. Dec 19/5

Dear Michael,

At the meeting of E(DL) on 17th March it was agreed that my Secretary of State should proceed with the reorganisation of the Royal Ordnance Factories as quickly as possible - and that an announcement should be made as soon as possible, in order to bring to end the present uncertainties (particularly in the minds of employees) over the future of the ROFs. Your letter of 25th March to Peter Jenkins at the Treasury signified that the Prime Minister was content with this course of action.

My Secretary of State has thought it right, in view of other defence preoccupations and concerns, not to make the announcement during recent weeks. But Mr Nott now feels that there is no reason for further delay; and he has accordingly decided that the announcement should be made by means of a written Parliamentary Answer this Thursday, 20th May.

I enclose the text of the Answer, which has been prepared in consultation with the Treasury, and which will be given as a pursuant to the oral Question from Jack Straw MP on 27th April when he was told that we hoped to make a statement in the near future. Copies of the text, with a short covering letter from Lord Trenchard, will be given to all MPs with a constituency interest at about 3.30 p.m on 20th May.

I am sending copies of this letter to the Private Secretaries to other members of the Cabinet; and to Murdo Maclean (Chief Whip's Office) and David Wright (Cabinet Office).

Yours ever,

David T Piper

(D T PIPER)

M C Scholar Esq

CONFIDENTIAL

PARLIAMENTARY ANSWER ON 20 MAY 1982

During recent months, the Government has considered carefully the best way of making changes to the constitution of the Royal Ordnance Factories, in order to ease the existing constraints on their operations and to allow them to function more competitively.

We have now decided that, subject to Parliamentary approval, the ROFs should no longer operate under the Government Trading Funds Act, 1973, but in a more commercial environment under the Companies Acts. The necessary legislation will be introduced as soon as the Parliamentary timetable allows. Initially thereafter Government ownership will continue but with the intention in due course of involving private capital directly - either through sale to the private sector, joint venture or flotation of shares. Meanwhile, in line with the recommendations of the 1981 Study Group report, relevant MOD design and development capabilities and sales functions will be transferred to ROF control as soon as possible. The Government believes that this represents a constructive and purposeful programme for the development of the Royal Ordnance Factories beyond their present status.

The cooperation of existing staff at all levels is vital for the success of the ROFs both during the transitional period and when Companies Act status is achieved; and the need is well recognised for early discussions with the Trade Unions concerned on the terms and conditions of service to apply on the change of status. Further details will be made available as soon as possible to ensure that the transition is effected smoothly and that, in the meantime, the business of the ROFs is carried out and developed efficiently and energetically.

bcc John Vereker

*See Mac*

10 DOWNING STREET

From the Private Secretary

25 March 1982

Royal Ordnance Factories

The Prime Minister has seen the Chancellor's minute of 24 March about the conclusions of the Sub Committee on Disposal of Public Sector Assets about the future of the Royal Ordnance Factories.

The Prime Minister is content with the Sub Committee's conclusion that the Secretary of State for Defence should proceed with reorganisation of the Royal Ordnance Factories as quickly as possible, with the form and pace of the changes depending in part on when they can be converted into Companies Act companies. She agrees that the Secretary of State should announce his intentions as soon as possible so as to bring to an end the present uncertainties.

I am sending copies of this letter to the Private Secretaries to the other members of the Cabinet; and to Murdo Maclean (Chief Whip's Office), Gerry Spence (CPRS) and David Wright (Cabinet Office).

M. G. SCHOLAR

Peter Jenkins, Esq.,
H.M. Treasury.

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BK



Prime Minister

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Agree to the

approach in para 5,

Yes

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

discussion on timing of

legislation - planned for

Cabinet on 22 April (if there

is to be no Bill in 82-83 the pace

of change cannot be very quick) ?

PRIME MINISTER

ROYAL ORDNANCE FACTORIES

At their meeting on 17 March the Sub Committee on Disposal of Public Sector Assets (E(DL)) discussed a paper by the Secretary of State for Defence on the future organisation of the ROFs (E(DL)(82)1). I undertook to report the outcome of the discussion to you. It is relevant to the Cabinet's consideration of the 1982-83 legislative programme.

MCS 24/3

2. Following consultations with a wide range of firms, and advice from Rothschilds, it is clear that there is no serious private sector interest in buying the whole, or substantial parts, of the ROFs in the near future. The fact is that the ROFs are not currently a commercially attractive proposition: they operate as a Civil Service production organisation with no R & D base and no sales and marketing arm; they just about break even but their future workload is uncertain. It might be possible to sell one, or perhaps two, of the profitable factories now but E(DL) agreed with the Secretary of State for Defence that this would be a mistake since we would then be left with an incomplete and commercially unattractive organisation which would be very difficult to transfer from the public sector.

3. We agreed with the Secretary of State that the right course was to re-organise the ROFs so as to put them on a better footing for disposal later. Quite apart from the disposal



question, the ROFs badly need reorganisation and improvements in management and it is possible to make useful progress in that direction without legislation. But we agree that the aim should be, when a legislative opportunity arises, to convert the ROFs, together with associated R & D and sales operations, into three or four Companies Acts companies. We believe that opportunities could then be considered for the sale of the individual companies, or partnership arrangements between them and the private sector, and that this would reduce the risk that progress towards privatisation could be impeded by difficulties in breaking up a large single company, as with British Leyland. ROF staff would cease to be civil servants, though for the time being they would continue to be employed in companies wholly owned by the Government. There would be some public expenditure costs, mainly because of the need to transfer accrued pension rights to a new scheme, and the Chief Secretary would need to consider this further with the Secretary of State for Defence.

4. The present position on the timing of legislation is that the Home Secretary, as Chairman of QL, has advised the Secretary of State for Defence that he does not propose to recommend inclusion of a Bill dealing with the ROFs in the 1982-83 Session. The Secretary of State has told him that his own view remains that the prospect of early legislation would be a valuable stimulus to reorganisation and helpful in securing new top management to ensure a more commercial approach; he will wish to put forward this view when Cabinet discusses the 1982-83 programme.

5. Subject to your views, and to a decision on the timing of the legislation, we agreed that the Secretary of State for Defence should proceed with reorganisation of the ROFs as quickly as possible, with the form and pace of the changes depending in part on when they can be converted into Companies Act companies. He would announce his intentions as soon as



possible so as to bring to an end the present uncertainties, particularly in the minds of the employees, over the future of the ROFs.

6. I am sending copies of this minute to the Secretary of State for Defence, to the other Members of Cabinet and the Chief Whip, and to Mr. Ibbs and Sir Robert Armstrong.

G.H.

24 March 1982



POST OFFICE



IN
COMBINATION



MO 10/4

Gen MacL.
J.M.A.

MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1
Telephone 01-~~9307822X~~ 218 2111/3

28th July 1981

Dear John,

PRIVATISATION OF ROYAL ORDNANCE FACTORIES

My Secretary of State was grateful for your Secretary of State's letter to him of 17th July (received here on 22nd July).

Mr Nott takes Mr Biffen's point: he will ensure that the Department of Trade and the Office of Fair Trading are informed at the appropriate stages of the development of his thinking.

I am sending copies of this letter to Tim Lankester (No 10), Paula Diggle (HM Treasury) and David Wright (Cabinet Office).

Yours sincerely
Brian Nott

(B M NORBURY)

J Rhodes Esq

28 JUL 1981

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*Booth Mac**From the Secretary of State**R..*

The Rt Hon John Nott MP
Secretary of State for Defence
Ministry of Defence
Whitehall
London, SW1A 2HB

17 July 1981

*207**Dear John,*

PRIVATISATION OF ROYAL ORDNANCE FACTORIES

I have seen the recent exchange of correspondence about your proposals for the privatisation of the Royal Ordnance Factories. I think that it is appropriate at this stage to remind you that privatisation of these Factories, like similar earlier disposals, could carry implications for the mergers provisions of the Fair Trading Act 1973 and for my responsibilities together with those of the Director General of Fair Trading, under these provisions.

If any existing enterprise acquired shares sufficient to put in into a position to exercise material influence or control over the policies of the new company or companies, this could result in a qualifying merger situation arising which would then have to be considered for possible reference to the Monopolies and Mergers Commission under usual procedures. This does not mean that any options currently under consideration should be ruled out, but only that you should be aware of the necessity to keep me and the Office of Fair Trading informed of developments.

I am copying this letter to other members of the Cabinet, to Nigel Lawson and Michael Jopling, and to Sir Robert Armstrong.

John Biffen

JOHN BIFFEN

20 JUL 1987





*Govt
Moral*

Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon John Nott MP
Secretary of State for Defence
Ministry of Defence
Main Building
Whitehall
LONDON
SW1

13 July 1981

12/13/17

Dear John

THE ROYAL ORDNANCE FACTORIES

Thank you for your letter of 30 June about the next phase of work on options for the "privatisation" of the Royal Ordnance Factories.

As you know from my letter of 18 June, I am uneasy about the "joint company" option which you currently favour. It is far from clear that the new companies could be classified to the private sector: they would certainly have to satisfy stringent criteria of independence from Government before one could regard their future capital requirements as outside the PSR, and treat as receipts, rather than public sector borrowing, the proceeds from a sale of their shares. And it is far from clear that selling shares in "joint companies" is the course most likely to maximise financial returns.

I note that you are now asking merchant banks for advice on the feasibility of the "joint company" option, and I am grateful for your undertaking to keep me in touch with progress. But I have to say that it seems to me rather unlikely that an appraisal concentrating on that option alone could be regarded as a basis for firm Government decisions on how best to privatise the Ordnance Factories. In his letter to you of 23 June Keith Joseph envisaged discussion in E(DL): I believe that we shall then need an appraisal of the feasibility and financial implications of all the various options. It would reduce the risk of further future delays if you could see your way to commission this work too before too long.

Copies of this letter go to the other recipients of yours.

Yours faithfully
NIGEL LAWSON *1981*

13 JUL 1981



ef

Ministry of Defence
Council of Civil Service Unions

No ack Govt by Madam
MA 3/11

Chairman G LEWTAS
Secretary H E BREYLEY ext 4174

Room 467
Old War Office Building
Whitehall
London SW1A 2EU

Deputy Secretaries
J HIGGINS ext 0819
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H D C O'KANE ext 0602
ext 4710
Mrs M J THURSTON ext 4875

Telephone:
01 218 (Direct Dialling)
01 218 9000 (Switchboard)

Your Ref:
Our Ref: 24/170

Rt. Hon Margaret Hilda Thatcher MP

1 July 1981

Dear Mrs Thatcher

GOVERNMENT PROPOSAL TO PRIVATISE THE
ROYAL ORDNANCE FACTORIES

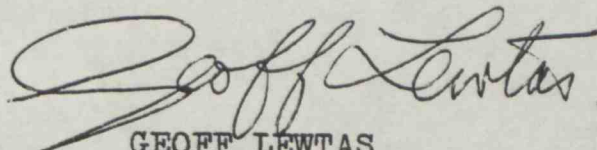
The Secretary of State gave a Written Answer to a Parliamentary question on 25th June concerning the outcome of the Study set up in October 1980. The Study Group's Consultative Document was made available to MPs a few weeks ago but the more recent Written Answer to a PQ has demonstrated that the Government are definitely in favour of privatisation, although the form that this will take is still unclear.

The Unions view this prospect with anger because it represents an opinion based on dogma and doctrinaire views which cannot properly be applied to the ROFs. We spell out in the attached pamphlet our reasons for opposing the proposal and we sincerely hope you will read it.

We believe that the survival of the ROF organisation as a single entity is essential for its continuing efficiency and profitability and to ensure that its customers can be offered suitable sales packages with the necessary support and back-up services.

We ask you to make clear your opposition to the privatising concept and to ensure that any legislation receives the same treatment.

Yours sincerely



GEOFF LEWTAS
Chairman, MOD CCSU

THE ROYAL ORDNANCE FACTORIES

THE ISSUE

The Government initiated a study as follows:

'The Study should consider all possible lines of future development for the Royal Ordnance Factories (ROF) Organisation, *in particular the scope for privatisation* and should recommend whether one or more of these should be adopted in preference to continuation as a Trading Fund.'

THE FACTS

The Royal Ordnance Factories which have a history and tradition of service to the Crown stretching over hundreds of years—now constitutes a large engineering and chemical manufacturing organisation. Eleven Royal Ordnance Factories were in operation during the year: seven engineering factories, two ammunition filling factories and two explosives factories. The average number of people employed during the year was 22,084 and their remuneration was £99,033,000.

The Organisation is a corporate one and manufacture of a particular equipment or store usually involves several factories. It is amongst the more important Ministry of Defence contractors and is a major supplier of the Army, providing about one-sixth of its equipment (by value). The Organisation is the Services' preferred source of supply for a large part of its range of manufacture and in many cases is the only UK supplier.

The Task is to meet the munitions requirements of the Services and undertake approved work of a defence nature for Commonwealth and other friendly Governments. Commercial work is undertaken to assist in maintaining essential defence capacity.

The Operation From July 1 1974, in accordance with the Royal Factories Trading Fund Order 1974 made under the Government Trading Funds Act 1973, the operations of the Royal Ordnance Factories have been financed by means of a trading fund instead of by annual votes and appropriations. The organisation remains under the control and management of the Secretary of State for Defence and is required to pay for all supplies of goods and services received and to charge for all supplies of goods and services both to government departments and to other customers at home and abroad.

Performance—In purely financial terms, the ROF Organisation has been very successful. It has not needed to have recourse to public funds at any time since the inception of the Trading Fund, being well able to generate its own funds for investment and expansion. It has regularly met the financial objective set; paid interest charges as scheduled; and taken the initiative in paying off early a large proportion of the originating debt from the National Loans Fund. The ROFs have distributed £42m of profits to the Exchequer by way of dividends while retaining in the business a further £80m of non-distributed profits.

Capital expenditure has been steadily increasing over recent years and now amounts to some £30m per annum. Investment in modern machines has meant that the Organisation is now one of the foremost users of computerised numerically controlled machines in the United Kingdom.

THE UNIONS SAY

It is publicly recognised that the Royal Ordnance Factories have an outstanding record of success under the Trading Fund system and have managed to combine the ability to meet the needs of their prime customer with a substantial return to the taxpayer on his investment. The current Trading Fund has its deficiencies, but the organisation has shown its willingness to adapt to changing circumstances and indeed to anticipate future developments and plan accordingly. The organisation enjoys the support of a loyal committed workforce and Trade Unions sensitive to the needs of the organisation.

It would be foolish to deny that the Trading Fund has its limitations but more foolish still to jeopardise all that is worthwhile in the present system by hiving it off from the MOD and the Civil Service. The mere fact that a study with terms of reference so clearly biased towards privatisation has been commissioned has already caused considerable difficulties in maintaining the morale of staff.

The Mallabar investigation (The Mallabar Report—1971 Cmnd 4713) was far more comprehensive than this limited study can ever be. The report of that study concluded that privatisation had no real advantage over the Trading Fund. Although some time has elapsed since Mallabar we still support the views in that Report and believe that there are severe risks attaching to any consideration which would remove the production of essential munitions for the Armed Forces from the direct control of the Crown.

THE STUDY GROUP SAYS

We all recognise the success which the Royal Ordnance Factories Organisation has achieved since the setting up of the Trading Fund in 1974. Similarly we recognise the need for some change given the constraints which have been identified and the fact that the trading environment both at home and abroad has changed dramatically in the past two years.

We conclude that there are three main Options open for future development:

- (a) To improve the present Trading Fund Organisation by removing some of the impediments which we identified (Option I).
- (b) To dispose of the Organisation to the Private Sector either as a whole or in parts (Option II).
- (c) To turn the Organisation into a Companies Act structure in its own right and involve private capital flotation of shares of itself or of subsidiary companies (Option III).

We recognise that the Options are not exclusive and that it would be possible to move to Option II via Options I and III.

In considering the three options, the study group regarded the following points of principle as relevant:

- (a) If it is accepted that the Trading Fund would only be an interim stage of development, it could be argued that a move to privatisation should involve the organisation in its entirety. Among the reasons for privatisation as an entity is that the organisation is structured as an interdependent body and that the flexibility in operation which this structure gives is an argument against any degree of fragmentation.
- (b) On the other hand there are arguments for considering the privatisation of the ROF organisation in parts, either by selling off (Option 2) or under the umbrella of a Companies Act Holding Company (Option 3). The benefit in the 'selling off' approach is seen to be that, in the Option 3 case, this would be the best way of exposing the organisation to market forces and that in the Option 2 case, this would provide a less complicated solution.

THE UNIONS CASE

Deficiencies in present Organisation

The ROFs were not intended to be and therefore are not a Research and Development Organisation. This fact derives quite naturally from their task which is essentially to provide what the Armed Forces require, to the design required, to the standard required, at the time required. It is not to try to sell to the Forces the products which are most commercially viable.

To change this arrangement, whether by hiving-off or otherwise, would lead to a situation in which the Forces would have available only those munitions which were to a design and of a quality which were commercially acceptable. The producers would require the ability to refuse any order which did not meet this description. (The ROFs are currently unable to refuse an order from MOD). Any such change would require a fundamental re-evaluation of the role of the ROFs and their relationship to MOD. We believe firmly that it is essential that the Forces should retain the capability to order weapons which they require for operational reasons and should not be placed in a position where operational necessity becomes subordinate to commercial viability. This can be achieved under the Trading Fund but not otherwise.

ROF Sales

The Organisation's products have been remarkably successful in terms of exports and the Organisation has twice received the Queen's Award for export achievement. The loss of the major contracts with Iran has forced the organisation to seek new markets overseas and it would appear unlikely that a new series of contracts with one customer is likely to emerge as a direct replacement for the loss of the Iranian orders.

In seeking to establish new markets the ROFs are undoubtedly handicapped by a number of factors including their lack of R&D facilities and the requirement to adhere to MOD policies and procedures for overseas sales. Whilst it is essential that Parliament should continue through Ministers to exercise a direct control over the sale of armaments to foreign powers, this could readily be achieved

by giving the ROF organisation its own in-house sales organisation. This would enable control to be matched with commercial practice.

ROF Procurement

Again the Procurement Executive in MOD and Government Accounting procedures may be represented as straight jackets which prevent the organisation from operating freely in the market place. These constraints were not able to prevent situations in which Gunpowder once produced at home is now imported to the ROF organisation or the much publicised case of Chieftan tank components being supplied from Iron Curtain countries.

We would suggest that a slightly greater freedom on procurement practices would assist the organisation to maintain its viability in an ever more difficult environment but we believe that any relaxation of direct controls must take place in the knowledge that the way in which the ROFs conduct their business will continue to come under public and parliamentary scrutiny, by modification of the Trading Fund concept and not by its abandonment.

It is essential to the needs of the Armed Forces that the ROFs must not be allowed to enter into deals which would in any way prejudice their ability to fulfil their main task no matter how commercially attractive those deals might seem. Again it is the need to match control and commercial practice.

Personnel Management

Through delegated authorities the ROF organisation enjoys discretion on a number of personnel management issues e.g. in determining its own manning levels. It is able to apply to normal Civil Service practices the special considerations which apply under the Trading Fund.

By use of these authorities the organisation has been able to maintain flexibility which has by and large ensured that manpower levels have been very closely related to the current task. It is fair to claim that the Trades Unions, non-industrial and industrial, have co-operated with ROF HQ Personnel Managers in achieving a realistically staffed organisation.

However, the need to maintain a Civil Service structure of grades can be cited as a constraint which could be removed by hiving-off. It is doubtful whether the net effect of any such change would be of benefit to the organisation. The following points require consideration, when the issue of Civil Service constraints is under examination:

- (i) the retention of Civil Service grades can ensure there is a ready interchange between the ROFs and the various areas of expertise readily available in MOD. The ROFs are thus able to secure the services of employees with R&D, Management Accountant, ADP, Contracts/PE Personnel Management etc. backgrounds.
- (ii) The present similarity of structure between the ROFs and MOD facilitates this relationship.
- (iii) In areas such as Personnel Management, Accountancy, Employment of Professional and Technology staff, Administration and ADP the ROF organisation is not able to offer the same career structure as the Civil Service. The present ability to share in career opportunities elsewhere in the Civil Service could be removed by hiving-off the staffing of such areas and could demand the creation of a special structure or the introduction of different pay structures, personal promotions etc. All of these would force up overheads and prices and therefore the cost to the taxpayer.
- (iv) The organisation has been successful in converting different grading structures to Civil Service standards e.g. Labour Managers, Group Office and the reasons for having done so remain valid.

We would accept nevertheless, that there may be a need to review the application of Civil Service practices in the ROFs with a view to greater flexibility but we cannot accept that the complete abandonment caused by hiving-off would necessarily be to the long term advantage of the organisation.

THE STUDY GROUP'S CASE

Constraints on the present ROF Organisation—Despite the success of the Trading Fund to date and the close relationship which exists with the Ministry of Defence, the present arrangements create constraints on the ROFs' operations for the following reasons:

- (a) Lack of ROF control over export sales.
- (b) Shared responsibility for contracts and purchasing.
- (c) A separate design and development organisation.
- (d) Lack of ROF control over the personnel function.
- (e) Inability to purchase shares and set up joint companies.
- (f) Lack of access to ECGD facilities.
- (g) Public Sector financial constraints and scrutiny.

Exports

At the time of the Mallabar Report on the ROFs and the Royal Dockyards in 1971 only some 25% of ROF output was for overseas but the organisation responded to the challenge of their commercial status and continues to be an export-conscious organisation. Although relying largely on the Defence Sales Organisation for sales activity the ROFs have demonstrated their ability to operate commercially and about 10% of overseas sales are currently negotiated by ROF staff. Many of these contracts involve direct dealings with overseas companies in the armaments field. In addition ROF staff provide support to the Defence Sales Organisation and to International Military Services (IMS) and indeed have been involved in all recent major negotiations involving the sale of ROF equipment. But the primary responsibility for selling ROF products overseas lies with the Defence Sales

Organisation: sales promotion is undertaken by the geographical sales desks with support from the Sales Supply branch. This latter also produces the quotations for customers and is responsible for contract negotiations and the organisation of after sales support. IMS Ltd also carries out tactical selling of ROF products in certain markets.

The present arrangements are unsatisfactory in that they put the ROFs at one remove from the customer and tend to inhibit them from fully appreciating market requirements and how these might be satisfied.

Contracts

A significant part of the ROFs contract function is performed within the Organisation but the balance continues to be under the control of the Director General of Defence Contracts. This inhibits the development of a much closer link between the ROFs and their suppliers and customers.

Design and Development

Over the past few years the ROFs have steadily built up a design and development capability and now employ some 700 staff on this task. But the capability is uneven, ranging from full responsibility for research design and development for small arms systems to experimental workshop production for high explosive shell. Although a large proportion of design and development work on ROF produced equipment is undertaken in the MOD's R&D Establishments ROF involvement is maintained through the many joint project teams which exist and which were set up specifically to improve the relationship between design and development production. But there is a need for the ROFs to expand the range of capabilities particularly in the light of an increasing need for the ROFs to join with companies overseas in collaborative work. Greater ROF activity in this area would also allow the ROFs to apply a fuller part in meeting

British Service requirements and enhance their ability to manufacture special-to-type or to modify existing equipment for sale overseas.

Personnel

Although the ROFs have a large degree of autonomy delegated in respect of industrial employees, they are far more restricted in the case of non-industrial employees. More generally, the ROFs are currently counted within the overall total of Civil Service numbers in spite of the fact that the Organisation's response to markets has long been accepted as the most appropriate criterion for its level of manning.

Powers to fund the Purchase of Shares

Although the Secretary of State for Defence may purchase shares, the Government Trading Funds Act of 1973 does not permit ROF monies to be used to fund such purchases. The absence of the commercial flexibility to participate in joint company ventures or to take over other companies places the ROFs at a disadvantage at a time when there is an increasing trend towards collaborative projects, both nationally and internationally.

Export Credit Guarantee Department Facilities

These facilities, especially low interest credit are necessary ingredients of some export deals. But one Department of State cannot guarantee another so the credit and insurance cover available to commercial exporting organisations is not available to the ROFs.

Public Sector Constraints

There are a number of constraints which apply to the ROF Trading Fund simply because it is in the public sector. As noted above, its employees are Civil Servants; borrowing is a charge against the PSBR; and the fact that commercial decisions are open to E&AD and Public Accounts Committee scrutiny could be argued to have a generally

THE ROFS AND THE MINISTRY OF DEFENCE

THE UNIONS AND THE STUDY GROUP AGREE

Benefits accrue to both sides from the present relationship between the ROFs and the rest of the Ministry of Defence. As the preferred and often only UK source for a wide variety of equipment and stores, the ROFs guarantee the Ministry of Defence a production capability to meet national needs. This production capability has been maintained and indeed enhanced by heavy investment in new plant and machinery made possible by the ROFs' success in overseas trading. This investment not only allows the ROFs to meet British Service requirements for quality products in a cost effective manner but it also allows the home customer to benefit from the economies of scale by way of reduced unit prices and provides a significant contribution to cover MOD overheads. ROF speculative work for overseas sales also benefits the home customer because there is a read across into MOD projects; recent examples have been on Main Battle Tank and Tank Gun Ammunition. More generally the ROFs have continued to act as the standard to MOD for the price and quality of some defence stores against which to judge other procurement.

The ROFs currently benefit from the fact that the foreign trading risk has been largely carried by Ministry of Defence Votes, and not the Trading Fund, although no financial charge to MOD has arisen in practice since 1974 on this account. The ROFs are also able to draw, in a repayment basis, upon the services of the MOD Research and Development establishments, other MOD specialist services and the Defence Sales Organisation.

THE UNIONS PROPOSE:

A Modified Trading Fund

There is no doubt that both the organisation and the Council could find ways of improving the present trading fund for instance:

- (a) R&D—The ROFs should be involved far more in the research preceding development. Consideration should be given to the provision of an R&D facility within the ROF Trading Fund.
- (b) Procurement—the ROFs should have greater freedom in the procurement field to 'strike bargains' in the commercial field.
- (c) Pay and Complementing—A greater freedom in both these areas would have gone a long way in enabling the ROFs to solve recent problems. Certainly more flexibility in these areas would enable the staff in the ROFs to feel that they were fully part of the organisation and were being fairly compensated for their efforts.
- (d) Productivity—The factories have already been taking positive steps to increase productivity by means of the introduction of a new generation of sophisticated productivity deals for the industrial work place. It is perhaps too early to judge what effect these 'stage 2' schemes will have on the competitiveness of the organisation but this should be further considered.
- (e) New Technology—The organisation is also beginning to adopt the benefits of computer technology to deal with a variety of procurement production control, payroll and other systems and new systems are currently under test at RSAF Enfield—again with the co-operation of the non-industrial Trades Unions. The ROF Central Computer Bureau at Chorley is due to take on a new machine in 1981 to replace out-dated equipment and a variety of mini-computers are being introduced at the factories. The impact of new technology on the organisation's effectiveness will need to be taken into account in assessing the extent to which constraints should be removed.
- (f) Sales—The ROFs should have its own in-house sales organisation seeking new customers and maintaining contacts. This would ensure that all sales to foreign governments were still under the direct control of the Government.

There are other changes which could well result from studies and reviews taking place elsewhere in MOD and the Civil Service. We shall want to explore ways and means whereby these may impact upon the present trading fund and justify its modification.

THE STUDY GROUP PROPOSES:

(1) Options for Change

The Evolved Trading Fund:—The ROFs would remain as a Trading Fund organisation but certain measures could be taken to ameliorate the constraints identified in page 3. In essence these measures would be as follows:—

- (a) The ROFs would be given their own sales arm and it would appear that this objective is achievable in the short term by the transfer of functions currently exercised by the Defence Sales Support Division of the Defence Sales Organisation.
- (b) The ROFs would be given responsibility for the balance of the contractual work associated with ROF products.
- (c) In line with the recommendations of the review of the R&D Establishments the ROFs would take on more design and development work.
- (d) In the personnel field the ROFs would need to have greater control over the conditions and service of their staff. (The Mallabar Report visualised a special ROF Group within the Civil Service.)
- (e) An amendment to the Government Trading Funds Act of 1973 could be made to allow the ROFs to purchase shares and become involved as a risk-sharing partner both in consortium deals and manufacturing operations at home and abroad.
- (f) Legislation could be enacted deeming the ROFs not to be a Crown service so that the Organisation could have access to both ECGD cover and credit.

(2) Disposal to Private Industry

The assets of the ROFs could be sold off to private buyers on a factory by factory basis or in functional groups or the Organisation could be sold off in its entirety.

(3) Creation of a Companies Act Structure

The ROF Organisation could be given a Companies Act structure 100% Government owned. Subsequently it could either:—

- (a) itself move into private ownership through the sale of shares and relinquishment of Government control;

or

- (b) create subsidiary companies, each responsible for a part of the Organisation some or all of which would move into private ownership through the sale of shares.

NOW PARLIAMENT MUST SAY

The Study Group appointed by the Government has not made any recommendations in its report. It has produced a consultative document which gives options suggesting that some form of 'privatisation' is now needed; whether this be by way of 'selling off' or 'injecting' private capital into the organisation. The Government is intent on changing the form of the present organisation in a way in which there can be some involvement of private capital.

The Unions have told the Secretary of State that there is no such need. We allege it arises only because the ROFs are a profit making organisation. There have been no proposals from the Government to involve private capital in the MOD Royal Dockyards or the Research and Development Establishments; there having been similar studies into those two areas of the MOD.

WHY—because they do not and never will make a profit.

But there is another reason why the Government wants to remove the ROFs from the Civil Service. The Prime Minister decided that the staff in Ministry of Defence must be cut to 200,000 by 1 April 1984. This means that 32,000 jobs must now be eliminated. Given all the cuts that have taken place in MOD a further cut of this magnitude cannot be achieved without taking the ROFs out of MOD. The unions say that it would be fraudulent for a decision to be made on these grounds.

The real choice is:

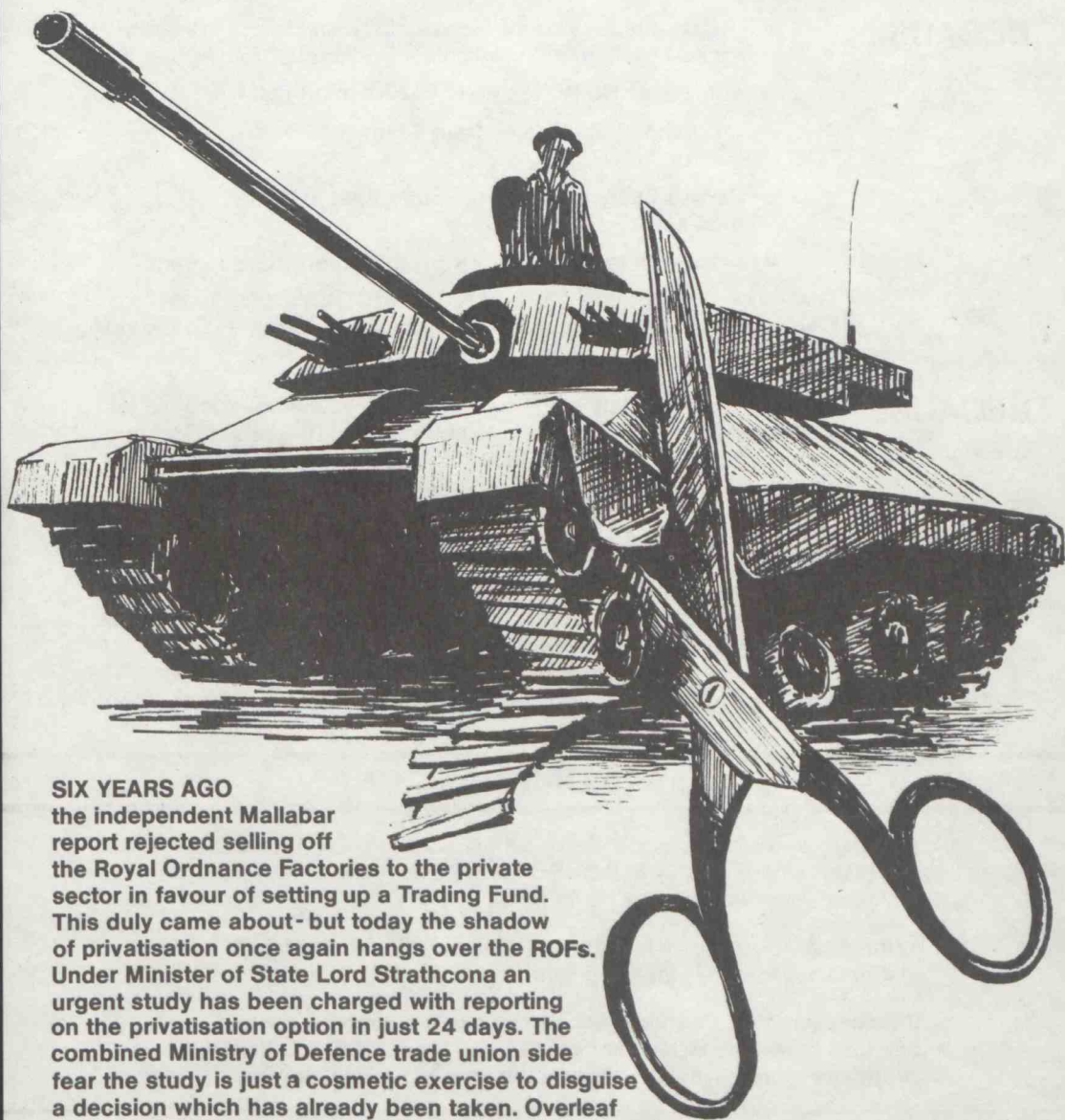
THE DOGMA OF GOVERNMENT *VERSUS* VALUE FOR MONEY.

MOD COUNCIL OF CIVIL SERVICE UNIONS

IN DEFENCE OF DEFENCE

THE CASE AGAINST

THE ROF AUCTION



SIX YEARS AGO

the independent Mallabar report rejected selling off the Royal Ordnance Factories to the private sector in favour of setting up a Trading Fund. This duly came about - but today the shadow of privatisation once again hangs over the ROFs. Under Minister of State Lord Strathcona an urgent study has been charged with reporting on the privatisation option in just 24 days. The combined Ministry of Defence trade union side fear the study is just a cosmetic exercise to disguise a decision which has already been taken. Overleaf the unions list their reasons why the ROFs should stay in public hands. We believe it is an unanswerable case.

Why the ROFs must not be privatised

BECAUSE THE nation's defence depends on **military** not **commercial** criteria. And only publicly-owned ordnance factories can guarantee Britain's armed forces that their weapons are built to win real battles and not price wars. In fact many specialised armaments are made at a loss - which is why the ROFs are not allowed to refuse an order placed by MOD.

BECAUSE THE ROFs have already won the battle for the marketplace. In the five years since their finances were put onto a Trading Fund footing they have

- **earned the British taxpayer £122m in profits**
- **more than tripled sales from £81m in 1974 to £284m in 1978**
- **earned £516m in exports - more than half their total sales**
- **twice won the Queen's Award for Export Achievement**

That is not a tax burden - that is tax relief! The 11 ROFs today more than pay their way worldwide by virtue of their quality, reliability and outstanding performance.

BECAUSE THE ROF success story is built on the committed teamwork of all its 22,000 employees. Each worker today adds twice the value to factory output that he earned in 1974. Essential to that effort is the reservoir of skills the ROFs can tap from the rest of the civil service - be it research and development, foreign military know-how, advanced computer technology etc.

BECAUSE THE Government can transfer 22,000 jobs to the private sector - but not their costs. First, breaking up the existing network of integrated expertise will disrupt efficiency. Second, it will drive up costs as any new owner will be forced to develop back-up facilities of his own. Third, a private owner will naturally strive to maximise his profit and so raise prices on goods he knows Government must buy.

A CASE FOR CHANGE?

ALL THIS poses the question: Why rewrite a success story? What can private enterprise provide that the ROFs cannot - in human resources, technical ability and financial performance?

All the Government will achieve is to give away public accountability for the £130m of public money invested in the ROFs over the last six years.

Privatisation does not make sense - unless it is simply a cooked-up exercise to reduce MOD numbers before 1 April 1984. It is hard to imagine a more costly sacrifice on the altar of political dogma.

FIGHT TO SAVE YOUR JOB SUPPORT YOUR LOCAL ACTION COMMITTEE

**Issued by the MOD Council of Civil Service Unions
on behalf of CPSA, SCPS, IPCS, CSU, AGSRO and FDA.**



Gore Mach.

MINISTRY OF DEFENCE WHITEHALL LONDON SW1A 2HS

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

MO 10/4

30th June 1981

Dear Nigel

THE ROYAL ORDNANCE FACTORIES

Thank you for your letter of 18th June. The Parliamentary Answer I gave on 25th June kept open the options for privatisation as you requested.

You suggest we now bring in a Merchant Bank. I agree that professional advice will be needed but it is not, in my view, necessary at this stage to ask for more than a view on the sort of companies who would be likely to be interested in forming joint companies with a single factory or with groups of factories and to bring to such new organisations some at least of the capabilities and skills which the ROFs at present lack.

We are moving ahead on this basis forthwith and we shall be continuing our discussions with the firms with whom we have already been in touch. I will keep you in touch with progress.

I am sending copies of this letter to the Prime Minister, Willie Whitelaw, Keith Joseph, Francis Pym and Christopher Soames; and Sir Robert Armstrong.

Yours ever

John Nott

The Rt Hon Nigel Lawson MP



Secretary of State for Industry

Cost Mach

DEPARTMENT OF INDUSTRY
ASHDOWN HOUSE
123 VICTORIA STREET
LONDON SW1E 6RB
TELEPHONE DIRECT LINE 01-212 3301
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23 June 1981

The Rt Hon John Nott MP
Secretary of State for Defence
Ministry of Defence
Main Building
Whitehall
London SW1

John Nott,

ROYAL ORDNANCE FACTORIES

I have seen a copy of your proposed statement on the future of the Royal Ordnance Factories. I have also seen Nigel Lawson's letter to you of 18 June.

I am in favour of your preferred option for disposal of the Royal Ordnance Factories through the establishment of more than one Companies Act companies. I am therefore content with your statement although you might consider adding a sentence at the end of paragraph 3 on the following lines:

"The increased commercial discipline which should result within the ROF's from the proposed changes should benefit them and the defence industry as a whole".

I agree with Nigel Lawson that it may be desirable to carry out more studies before we can take a final decision on the method of privatisation and E(DL) may well be the most appropriate forum to discuss the results. But I am convinced we should not lose momentum and that we ought to consider the details in E(DL) well before the summer recess. I am content to leave it to you and Nigel to agree on the best way of carrying these studies forward, although David Young would be only too pleased to assist where he can.

I am sending copies of this letter to recipients of yours of 5 June.

John Nott

CONFIDENTIAL



HOME OFFICE
QUEEN ANNE'S GATE LONDON SW1H 9AT

23 June 1981

Dear Brian

THE ROYAL ORDNANCE FACTORIES

The Home Secretary has seen the recent correspondence about the terms of the statement which your Secretary of State wishes to make on proposals for the privatisation of the Royal Ordnance Factories. He is anxious that the statement should not give any commitment, whether explicitly or by implication, to the introduction of legislation on the subject next Session. He therefore hopes that your Secretary of State would be willing to adopt the form of words suggested in David Heyhoe's letter to you of 22 June.

I am copying this letter to Tim Lankester (No. 10), Ian Ellison (Department of Industry), David Heyhoe (Office of the Chancellor of the Duchy), Jim Buckley (CSD), Terry Mathews and David Willetts (HM Treasury) and David Wright (Cabinet Office).

*Yours sincerely
C J Walters*

(C J WALTERS)

B M Norbury Esq

CONFIDENTIAL

24 JUN 1981





Treasury Chambers, Parliament Street, SW1P 3AG

B M Norbury Esq
 PS/Secretary of State for Defence
 Ministry of Defence
 Main Building
 Whitehall
 LONDON
 SW1

22 June 1981

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Dear Brian,

THE ROYAL ORDNANCE FACTORIES

With your letter of 19 June you sent me a revised version of the proposed announcement about the future of the Royal Ordnance Factories.

I understand that the following further changes have since been made:-

- (a) the first sentence of paragraph 2 has been expanded to refer to changes which would "allow the Royal Ordnance Factories, building on their proven and successful production capability, to operate ...";
- (b) in the first sentence of paragraph 3 the reference to "privatisation of the ROFs" has become "changes in the constitution of the ROFs";
- (c) the last sentence of paragraph 3 now refers to the sale of one or two factories, not companies;
- (d) the second sentence of paragraph 4 has been truncated, and now mentions only that the successful achievement of the changes depends on many factors "some of which have not yet been fully explored";
- (e) the penultimate sentence of paragraph 4 now refers to personnel issues that would arise in implementing any transition.

Thus amended, the statement creates no difficulties for the Financial Secretary. He particularly welcomes amendment (d), which removes language which would have appeared to pre-empt the Government's choice between the various options for the future of the Royal Ordnance Factories.

The Financial Secretary welcomes Mr Nott's offer of a talk at some future date about merchant bank views on the feasibility and financial implications of the options. He has however asked me to let you know that he thinks it important that E(DL) should be in a position to consider the choice on the basis of a full and formal merchant bank appraisal.

I am sending copies of this letter to the other recipients of yours.

*Yours sincerely,
David Willetts*

D L WILLETTS
Private Secretary

23 JUN 1981





Chancellor of the Duchy of Lancaster

22 June 1981

Dear John,

R,

I have now seen a copy of Nigel Lawson's letter to you of 18 June about your proposals for the privatisation of the Royal Ordnance Factories.

As you know, Cabinet decided on 11 June that a bill dealing with the privatisation of the ROFs should not be added to next Session's legislative programme. My Private Secretary has already been in touch with yours to ask that the commitment to legislation contained in your draft statement circulated on 16 June should be modified. I was therefore concerned to see Nigel's suggestion at the end of his letter that the question of legislation in this area should be looked at by Cabinet once again. While I share your wish to see the ROFs put on a sound and efficient footing, I have to stress that it is unfortunately not possible for legislative time to be found next session for all the measures which colleagues have supported.

I should therefore require some convincing that we should now consider changing a programme agreed as recently as 11 June. I should certainly expect any colleague who would nevertheless wish the case for adding a particular bill to next Session's programme to suggest at the same time what other measures might be dropped in order to make the necessary room. In the meantime, of course, the Cabinet's decision not to add a Bill on the ROFs to next Session's programme stands.

I am copying this letter to other members of the Cabinet, to Nigel Lawson and Michael Jopling, and to Sir Robert Armstrong.

Francis Pym
John Nott

FRANCIS PYM

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

23 JUN 1981





Chancellor of the Duchy of Lancaster

THE CHANCELLOR OF THE DUCHY OF LANCASTER
WHITEHALL, LONDON SW1A 1AA

22 June 1981

R.
MAP

Sir Brian,

THE ROYAL ORDNANCE FACTORIES

Thank you for sending me a copy of your letter of 19 June to David Willetts, together with a revised draft statement.

I have only one comment on the amended text. This concerns the last sentence of paragraph 4, where the Chancellor of the Duchy would like to see the reference to legislation deleted altogether or, alternatively, the sentence to be amended on the following lines:

"The Government looks forward to further consultation with those concerned on the broad proposals which I have outlined in this Statement and for which legislation would be necessary."

I am copying this letter to the recipients of yours.

Yours aw.
DCR

D C R HEYHOE
Private Secretary

B M Norbury Esq
Private Secretary to
The Secretary of State for Defence
Main Building
Whitehall
LONDON SW1

CONFIDENTIAL

Govt Mach



MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1
Telephone 01-3347082 218 2111/3

MSM

MO 10/4

19th June 1981

R

Dear David,

126

THE ROYAL ORDNANCE FACTORIES

My Secretary of State has seen the Financial Secretary's letter to him of 18th June commenting on his to the Chancellor of 5th June; and I have now received your letter to me of 18th June about the terms of a public statement.

My Secretary of State has asked me to point out that he has to steer a difficult course on this subject given the likely attitudes of the Departmental Trade Unions to privatisation, and particularly to the direct sale of any factories especially at a time when he will be having to announce unpalatable decisions about the future of several of the Royal Dockyards. He has, accordingly, asked me to circulate the enclosed further draft of the Statement he would like to make next week (the re-draft also reflects comments received from others) and to say that he hopes that the Financial Secretary could let him know during Monday that he is content.

On the point in the Financial Secretary's penultimate paragraph, about merchant bankers, Mr Nott has asked me to say that some soundings have already been taken; he can discuss this subject more fully with Mr Lawson at a later date.

I am sending copies of this letter and the re-drafted Statement to Tim Lankester (No 10), John Halliday (Home Office), Ian Ellison (Department of Industry), David Heyhoe (Office of the Chancellor of the Duchy), Jim Buckley (CSD), Terry Mathews (HM Treasury); and David Wright (Cabinet Office).

Yours sincerely
Brian Nott

(B M NORBURY)

D L Willetts Esq

CONFIDENTIAL

DRAFT STATEMENT ON FUTURE OF ROFs

The Government has now completed its initial consideration of the report of the Study Group on the future development of the Royal Ordnance Factories referred to in my answer to my hon Friend the member for Colchester on 5th June 1981 (Col 218, Vol 6, No 120).

2. The Government agrees with the Study Group that change should be introduced to allow the Royal Ordnance Factories to operate in a manner more akin in scope to other firms in the Defence industry. Such changes should be aimed at removing the problems caused by the ROF organisation not having its own sales arm, and being unable to negotiate the terms and conditions of service of its employees and not having its own design and development capability. This is the only means of developing the ROFs further to provide greater sales and job opportunities, to the benefit of defence.

3. The Government accordingly favours early privatization of the ROFs and, among the possible ways of achieving this, will be examining their vesting and flotation as one or more Companies Act companies and the creation of one or more joint companies with industry. We would transfer to such companies as much as possible of the

relevant design and development capabilities and facilities now located at certain Defence R&D establishments. The direct sale of one or two companies, should this prove sensible, is not excluded.

4. In deciding to move forward in this way, the Government is seeking to overcome the major constraints on the ROFs identified by the Study Group. It recognises however that the successful achievement of these changes depends on many factors not least whether private industry is willing to contribute its skills and experience to the undoubted production capability of the ROFs themselves. The personnel issues that will arise in implementing the transition from public to private sector status will be handled with understanding. The Government looks forward to further consultation with those concerned on the broad proposals outlined in this Statement whilst the Parliamentary legislation that would be necessary is being prepared.

19 JUN 1987



CONFIDENTIAL



3 PRS
Civil Service Department
Whitehall London SW1A 2AZ
01-273 4400

19 June 1981

The Rt Hon John Nott, MP
Secretary of State for Defence
Main Building
Whitehall
LONDON
SW1A 2HB

Dear John,

THE ROYAL ORDNANCE FACTORIES

In your minute of 5 June you sought my agreement to your making known, in your general statement on the defence programme next month, your intentions for the future status of the ROFs. Your Private Secretary has now circulated a draft of this statement.

It all seems fine to me. No doubt when making your statement you will have in mind what the Prime Minister said publicly - that changes we make must be 'consistent with sound management and value for money for the taxpayer'. I presume you feel you could defend your decision in this regard - including likely movement of prices for ROF products.

I am copying this letter to the recipients of yours.

Yours ever

Chris Toft

SOAMES

CONFIDENTIAL

19 JUN 1981





2/11

PRIVY COUNCIL OFFICE
WHITEHALL, LONDON SW1A 2BQ

Chancellor of the Duchy of Lancaster

18 June 1981

Dear Brian,

T.B.

Thank you for sending me a copy of your letter of 16 June to John Wiggins about your Secretary of State's proposed statement on the future of the Royal Ordnance Factories.

Could I offer two comments? On timing, the Chancellor of the Duchy has noted that no statement will be made until policy agreement to the proposals has been obtained in the normal way. On the substance of what might then be said, the Chancellor of the Duchy considers that the present draft text goes too far regarding the commitment to legislation, which of course has not been settled yet. He would prefer either to omit the reference to legislation altogether, or to redraft paragraph 3 on the following lines:-

"Accordingly, while not excluding the possibility of direct sale of one or more of the Factories, the Government will also pursue with the relevant parts of industry the possibility of forming three or four joint companies which would bring together associated ROF and industrial interests in a way beneficial to both. Any changes on these lines would, of course, require the introduction of legislation in due course."

The words "whilst Parliamentary legislation is being prepared" would then be deleted from the end of paragraph 4.

I am copying this letter to the recipients of yours, and to Murdo Maclean (Chief Whip's Office).

Yours ever,
David

D C R HEYHOE
Private Secretary

Brian Norbury, Esq
Private Secretary to the
Secretary of State for Defence

CONFIDENTIAL

10-11-1961





CONFIDENTIAL

DEPARTMENT OF INDUSTRY
 ASHDOWN HOUSE
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 SWITCHBOARD 01-212 7676

Secretary of State for Industry

18 June 1981

The Rt Hon John Nott MP
 Secretary of State for Defence
 Ministry of Defence
 Main Building
 Whitehall
 London SW1

Handwritten initials: N.

Handwritten signature: Ian John.

THE ROYAL ORDNANCE FACTORIES

I have seen a copy of your letter to Geoffrey Howe of 5 June.

As selling off the Royal Ordnance Factories may not be practicable I am content that you should pursue privatisation through the establishment of more than one Companies Act company along the lines you propose in your letter. This is clearly preferable to keeping the ROFs within the public sector but with a trading fund.

I have copied this letter to the recipients of yours.

Handwritten signature: Evan-Kerr

CONFIDENTIAL

19 JUN 1981





Govt Machinery

Treasury Chambers, Parliament Street, SW1P 3AG

B M Norbury Esq
 PS/Secretary of State for Defence
 Ministry of Defence
 Main Building
 Whitehall
 LONDON
 SW1

18 June 1981

Dear Brian,

R
1874

THE ROYAL ORDNANCE FACTORIES

You wrote to John Wiggins on 16 June with the draft of an announcement about the future of the Royal Ordnance Factories.

Your Secretary of State will by now have seen the Financial Secretary's reply of 18 June to his minute of 5 June. Given the importance of not prejudging the options, the Financial Secretary would prefer that paragraphs 3 and 4 of your draft be cast in more general terms, perhaps along the following lines:-

"The Government favours early privatisation of the ROFs, but has yet to decide what form this should take. We shall undertake an appraisal of the feasibility and financial implications of the various options, which include the direct sale of one or more of the Factories, the vesting and flotation of the ROFs as one or more Companies Act Companies, and the creation of one or more joint companies with industry. On the basis of this further work, the Government will table legislative proposals as soon as possible. Further consultations will be held with those concerned, and the personnel issues that will arise in implementing the transition from public to private status will of course be handled with understanding."

A copy of this letter goes to the other recipients of yours.

Yours sincerely,
 David Willetts

D L WILLETTS

18 JUN 1981





Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon John Nott MP
 Secretary of State for Defence
 Ministry of Defence
 Main Building
 Whitehall
 LONDON
 SW1

18 June 1981

THE ROYAL ORDNANCE FACTORIES (ROFs)

Geoffrey Howe has asked me to reply to your minute of 5 June about how best to "privatise" the Royal Ordnance Factories. You envisage a series of three or four companies, each specialising in one area of ROF activity, whose equity would be shared between HMG and relevant parts of industry.

We strongly support the principle of privatising the ROFs at an early date. Like you, we think it anomalous that this element of the UK defence industry should remain in the public sector. We also recognise your need to secure staff savings before 1 April 1984 to contribute to the target for Civil Service manpower reductions.

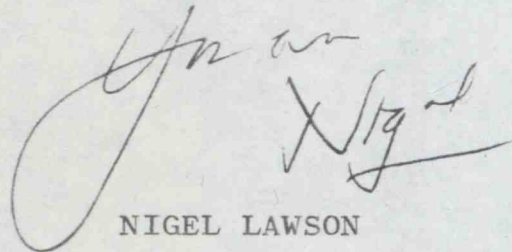
But we are not yet clear that the particular proposal you put forward is necessarily the right answer. You do not say, for instance, what degree of private sector participation you envisage, or whether you intend to relinquish Government control over the companies. These issues are of course crucial to classifying the new companies to the private sector.

The ideal outcome of any privatisation exercise, of course, is an independent commercial company, with no Government shareholding. Such an outcome best fulfills our policy objectives, and also maximises the benefit to the Exchequer. If a case for retaining a Government shareholding is accepted, it becomes necessary to commit the Government, by means of an early statement, not to vote its shares or otherwise influence the new companies' commercial policies on investment, borrowing, pricing and the like. Plainly, in these circumstances, a low shareholding and minimal or no rights for the Government to appoint Directors, best substantiates the Government's renunciation of control.

More generally, the Treasury concern in examining your proposals is that the net receipts to the Consolidated Fund should be maximised. This will be particularly important given the close match between net asset values and the public expenditure implication of the accrued pension rights of ROF employees, although the latter should not of itself deter us from seeking long term savings. The option you propose may well prove the best, but we would prefer not to take a final view until you have taken professional advice on the various options available. These should include the sale of the ROFs to well-established private sector companies already in the defence industry field.

With this in mind, we suggest that any early announcement - and draft legislation - should be couched in general terms. We would not wish you to exclude any option which further study might prove attractive. Meanwhile, we should like to see merchant banks brought in to conduct an early appraisal of the feasibility and financial implications of the various privatisation options. Policy approval for the best route to privatisation of the ROFs, and for the necessary legislative powers, could then be sought from E(DL) Committee on the basis of this financial appraisal. And if E(DL) concur, you might then be in a position to invite Cabinet to reconsider its decision on 11 June that no room for a ROFs Bill should be found in the 1981-82 legislative programme.

Copies of this minute go to the other recipients of yours.

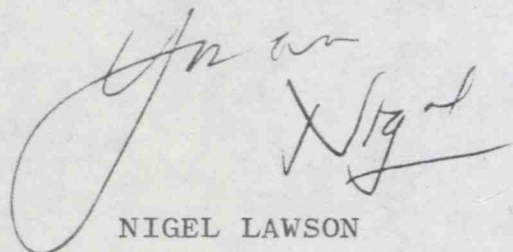


NIGEL LAWSON

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With this in mind, we suggest that any early announcement - and draft legislation - should be couched in general terms. We would not wish you to exclude any option which further study might prove attractive. Meanwhile, we should like to see merchant banks brought in to conduct an early appraisal of the feasibility and financial implications of the various privatisation options. Policy approval for the best route to privatisation of the ROFs, and for the necessary legislative powers, could then be sought from E(DL) Committee on the basis of this financial appraisal. And if E(DL) concur, you might then be in a position to invite Cabinet to reconsider its decision on 11 June that no room for a ROFs Bill should be found in the 1981-82 legislative programme.

Copies of this minute go to the other recipients of yours.



NIGEL LAWSON

18 JUN 1981





MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1
Telephone 01-~~922XXXX~~ 218 2111/3

MO 10/4

Prime Minister

16th June 1981

Dear John,

Mr Nott seeks clearance for an announcement on ROF privatisation. It could be a written answer on the day of the major statement; or in shorter form - a passage in the White Paper. Content with line of draft?

THE ROYAL ORDNANCE FACTORIES

Yes not MAF 17/1

in Parliament
operation

My Secretary of State minuted the Chancellor on 5th June concerning the future of the Royal Ordnance Factories; and Cabinet subsequently (on 11th June) agreed that, once policy had been decided, a public announcement could make clear that the Government was considering the preparation of the necessary legislation.

As he explained in his minute, my Secretary of State would like to make an announcement in conjunction with his general statement on the reshaping of the defence programme; and he would accordingly be very glad to know by close of play this Thursday whether the Chancellor would be content with the terms of the attached draft. He apologises for the inescapably short notice.

I am sending copies of this letter, and of the draft announcement, with the request that they offer any comments within the same timescale, to Tim Lankester (No 10), John Halliday (Home Office), Ian Ellison (Department of Industry), David Heyhoe (Office of the Chancellor of the Duchy), Jim Buckley (CSD), Terry Mathews (HM Treasury); and David Wright (Cabinet Office).

Your sincerely
Brian Nott

(B M NORBURY)

A J Wiggins Esq

DRAFT STATEMENT ON FUTURE OF ROFs

The Government has now completed its initial consideration of the report of the Study Group on the future development of the Royal Ordnance Factories referred to in my answer to my hon Friend the member for Colchester on 5th June 1981 (Col 218, Vol 6, No 120).

2. The Government agrees with the Study Group that change should be introduced to allow the Royal Ordnance Factories to operate in a manner more akin in scope to other firms in the Defence industry. Such changes should be aimed at removing the problems caused by the ROF organisation not having its own sales arm, and being unable to negotiate the terms and conditions of service of its employees and not having its own design and development capability. This is the only means of developing the ROFs further to provide greater sales and job opportunities, to the benefit of defence.

3. Accordingly, while not excluding the possibility of direct sale of one or more of the factories, the Government will as soon as possible table legislative proposals before Parliament seeking powers to convert the ROFs into one or more Companies Act companies; and meanwhile it will pursue with the relevant parts of industry the possibility of forming 3 or 4 joint companies which would bring together associated ROF and industrial interests in a way beneficial to both.

4. In deciding to move forward in this way, the Government is seeking to overcome the major constraints on the ROFs identified by the Study Group. It recognises however that the successful achievement of these changes depends on many factors not least whether private industry is willing to share in such a partnership, contributing its skills and experience to the undoubted production capability of the ROFs themselves. The personnel issues that will arise in implementing the transition from public to private sector status will be handled with understanding. The Government looks forward to further consultation with those concerned on the broad proposals outlined in this Statement whilst Parliamentary legislation is being prepared.

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17 JUN 1981

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Ref: A05060

Prime Minister

To note at this stage

~~MR ALEXANDER~~

M

for

And

The Royal Ordnance Factories

The Secretary of State for Defence sent the Prime Minister a copy of his minute dated 5 June concerning the report of the Royal Ordnance Factories' study group and the matter was also discussed in Cabinet on 11 June in relation to the Legislation Programme. At present I suggest that the Prime Minister need only take note of the course of action which the Secretary of State for Defence is proposing to pursue, and await the comments of colleagues to whom the minute is copied, and particularly of the Chancellor of the Exchequer, the Secretary of State for Industry and the Chancellor of the Duchy. I am inclined to suggest that a copy of the minute should also be sent to the Secretary of State for Employment, since the unions have had copies of the study group report.

2. The existence of the Royal Ordnance Factories as Government industrial establishments is due to the view taken by successive governments that it was in the national interest to ensure the preservation of industrial capacity in certain defence industries of which the continued existence in the private sector could not be guaranteed. At its peak during the last war the ROFs employed more than half a million people.

3. In peacetime the ROF organisation has tended to be a somewhat uncomfortable adjunct to central government. It is not the sole supplier of equipment to the armed forces, and a high proportion of its products are sold abroad. Hence in many areas it is in direct competition with private industry, and Civil Service conditions of service do not always appropriately meet its staffing requirements.



4. The Defence Secretary's proposal to change the status of the ROF organisation to that of a Companies Act company (or several such companies) with the equity initially held 100 per cent by government but with the possibility of flotation later, could solve many of these difficulties as well as being in keeping with the Government's broad political aim of reducing the size of the public sector.

5. The Secretary of State for Defence is likely to be pressed to declare his intentions when he is next top for questions on 23 June. The Cabinet agreed yesterday that, if the policy was agreed the Secretary of State should be free to say that it would be the Government's intention to introduce legislation in due course, without being specific about the precise timetable.

RA

ROBERT ARMSTRONG

12 June 1981

CONFIDENTIAL

Mr Palmer. NBPM? wh
A 7/6



MINISTRY OF DEFENCE
MAIN BUILDING WHITEHALL LONDON SW1
Telephone 01-~~XXXXXX~~ 218 2111/3

MO 10/4

9th June 1981

Dear John,

THE ROYAL ORDNANCE FACTORIES

My Secretary of State minuted the Chancellor of the Exchequer on 5th June about the future of the Royal Ordnance Factories.

I now enclose the report of the Study Group on the Status of the Royal Ordnance Factories in the form it has been given to the Departmental Trade Unions and will be placed, later this week, in the Library of the House of Commons.

I am sending copies of this letter and of the Report to Tim Lankester (No 10), John Halliday (Home Office), Ian Ellison (Department of Industry), David Heyhoe (Office of the Chancellor of the Duchy), Jim Buckley (CSD), Terry Mathews (HM Treasury); and David Wright (Cabinet Office).

Yours sincerely
Brian North

(B M NORBURY)

A J Wiggins Esq

CONFIDENTIAL

11



19 JUN 1984

SGS/ROF Consultative Document

REPORT OF
THE STUDY GROUP
ON THE STATUS OF
THE ROYAL ORDNANCE FACTORIES

REPORT OF THE STUDY GROUP ON THE STATUS OF THE ROYAL ORDNANCE FACTORIES

TERMS OF REFERENCE

1. The Terms of Reference of the Study Group were as follows:-

"The Study should consider all possible lines of future development for the Royal Ordnance Factories (ROF) Organisation, in particular the scope for privatisation and should recommend whether one or more of these should be adopted in preference to continuation as a Trading Fund."

The composition of the Study Group is set out at Annex A.

GENERAL

2. The Royal Ordnance Factories - which have a history and tradition of service to the Crown stretching over hundreds of years - now constitutes a large engineering and chemical manufacturing organisation. It currently employs some 21,000 people; there are 11 ROFs (manned by civil servants) and two agency factories run by industry under the Organisation's control. The Organisation's principal activities are the manufacture of ammunition and explosives (currently about 60% of its work); armoured fighting vehicles; guns and small arms; electronics and guided weapons components; and engineers' equipment.

3. The Organisation is a corporate one and manufacture of a particular equipment or store usually involves several factories. It is amongst the more important Ministry of Defence contractors and is a major supplier of the Army, providing about one-sixth of its equipment (by value). The Organisation is the Services' preferred source of supply for a large part of its range of manufacture and in many cases is the only UK supplier. A detailed note on the ROF Organisation, its factories, and the composition and Terms of Reference of the ROF Board and a note on the Trading Fund are at Annex B.

ROF PERFORMANCE UNDER THE TRADING FUND

4. The ROFs have performed very successfully since the introduction of the Trading Fund in July 1974 and related changes in autonomy and management structure. In manufacturing and sales terms, output increased in value from £103M in 1974/75 to £284M in 1978/79, representing a substantial increase in real terms for both the British Services and overseas customers. At the same time the proportion of total production for overseas customers increased until by 1976/77 it was over one half, an encouraging indication of the Organisation's competitiveness which earned the Queen's Award for Export in both 1976 and 1978. But in the last two years there has been a change in the ROFs' fortunes caused mainly by the loss of the most

important Iranian market but aggravated by disruptive action by non-industrial staff during 1979 and 1980. Output in real terms fell from £328M in 1977/78 to £319M in 1978/79 and to £278M in 1979/80. The forecast for 1980/81 is £240M. During the same period the percentage of sales attributable to exports fell from 53% in 1977/78 to a forecast 30% this year. More recently the reduction in Ministry of Defence orders has contributed to a further as yet unquantified reduction in activity. The numbers employed fell from almost 23,000 in April 1979 to a forecast 21,000 in April 1981. Nevertheless, the Organisation has coped with the consequential redundancies and reduced activity better than might have been hoped and the Organisation's financial strength has enabled it to mitigate the effects.

5. The Organisation has also demonstrated its management strengths since the introduction of the new arrangements. Generally, the restructured ROF Board and the revised Headquarters structure, coupled with increased delegated powers and the disciplines of cash flow and a financial objective, have proved of immense benefit in controlling and planning the use of resources. A comprehensive corporate plan has been drawn up annually. And apart from managing a heavier and broader manufacturing programme, a substantial capital investment programme, involving all factories, has been planned, executed and funded. Design and development facilities have also been increased. Further, the Organisation successfully undertook the overall project management of the Iranian tank project, which tested the engineering, planning, financial and contractual skills of the Organisation over a long period. Again, the Organisation has been engaged in large speculative projects, in developing new equipment - or modifying equipment to suit customers - for sale overseas: principal examples are the new FSAPDS shell and 81mm mortar system modified for the Americans. The ROFs have also displayed their business acumen, in conjunction with the Defence Sales Organisation, in working out comprehensive arrangements for substantial pre-funding and advances, in negotiating with overseas customers.

6. In purely financial terms, the ROF Organisation has also been very successful. It has not needed to have recourse to public funds at any time since the inception of the Trading Fund, being well able to generate its own funds for investment and expansion. It has regularly met the financial objective set; paid interest charges as scheduled; and taken the initiative in paying off early a large proportion of the originating debt from the National Loans Fund. The ROFs have distributed £42M of profits to the Exchequer by way of dividends while retaining in the business a further £80M of non-distributed profits. A graphical representation of the ROFs' Trading Fund performance is at Annex C.

THE ROFs AND THE MINISTRY OF DEFENCE

7. Benefits accrue to both sides from the present relationship between the ROFs and the rest of the Ministry of Defence. As the preferred, and often only UK source for a wide variety of equipment and stores, the ROFs guarantee the Ministry of Defence a production capability to meet national needs. This production capability has been maintained and indeed enhanced by heavy investment in new plant and machinery made possible by the ROFs' success in overseas trading. This investment not only allows the ROFs to meet British Service requirements for quality products in a cost effective manner but it also allows the home customer to benefit from the economies of scale by way of reduced unit prices and provides a significant contribution to cover MOD overheads. ROF speculative work for overseas sales also benefits the home customer because there is a read across into MOD projects; recent examples have been on Main Battle Tank and Tank Gun Ammunition. More generally the ROFs have continued to act as the standard to MOD for the price and quality of some defence stores against which to judge other procurement.

8. The ROFs currently benefit from the fact that the foreign trading risk has been largely carried by Ministry of Defence Votes, and not the Trading Fund, although no financial charge to MOD has arisen in practice since 1974 on this account. The ROFs are also able to draw, on a repayment basis, upon the services of the MOD Research and Development establishments, other MOD specialist services and the Defence Sales Organisation.

CONSTRAINTS ON THE PRESENT ROF ORGANISATION

9. Despite the success of the Trading Fund to date and the close relationship which exists with the Ministry of Defence, the present arrangements create constraints on the ROFs' operations for the following reasons:-

- a. Lack of ROF control over export sales.
- b. Shared responsibility for contracts and purchasing.
- c. A separated Design and Development Organisation.
- d. Lack of ROF control over the personnel function.
- e. Inability to purchase shares and set up joint companies.
- f. Lack of access to ECGD facilities.
- g. Public Sector financial constraints and scrutiny.

10. a. Exports

At the time of the Mallabar Report* on the ROFs and the Royal Dockyards in 1971 only some 25% of ROF output was for overseas but the Organisation responded to the challenge of their commercial status and continues to be an export-conscious organisation. Although relying largely on the Defence Sales Organisation for sales activity the ROFs have demonstrated their ability to operate commercially and about 10% of overseas sales are currently negotiated by ROF staff. Many of these contracts involve direct dealings with overseas companies in the armaments field. In addition ROF staff provide support to the Defence Sales Organisation and to International Military Services Ltd (IMS) and indeed have been involved in all recent major negotiations involving the sale of ROF equipment. But the primary responsibility for selling ROF products overseas lies with the Defence Sales Organisation: sales promotion is undertaken by the geographical sales desks with support from the Sales Supply branch. This latter also produces the quotations for customers and is responsible for contract negotiations and the organisation of after sales support. IMS Ltd also carries out tactical selling of ROF products in certain markets.

The present arrangements are unsatisfactory in that they put the ROFs at one remove from the customer and tend to inhibit them from fully appreciating market requirements and how these might be satisfied.

b. Contracts

A significant part of the ROFs' contract function is performed within the Organisation but the balance continues to be under the control of the Director General of Defence Contracts. This inhibits the development of a much closer link between the ROFs and their suppliers and customers.

c. Design and Development

Over the past few years the ROFs have steadily built up a design and development capability and now employ some 700 staff on this task. But the capability is uneven, ranging from full responsibility for research, design and development for small arms systems to experimental workshop production for high explosive shell. Although a large proportion of design and development work on ROF produced equipment is undertaken in the MOD's R&D Establishments ROF involvement is maintained through the many joint project teams which exist and which were set up specifically to improve the relationship between design and development production. But there is a need for the ROFs to expand the range of capabilities particularly in the light of an increasing need for the

ROFs to join with companies overseas in collaborative work. Greater ROF activity in this area would also allow the ROFs to apply a fuller part in meeting British Service requirements and enhance their ability to manufacture special-to-type or to modify existing equipment for sale overseas.

d. Personnel

Although the ROFs have a large degree of autonomy delegated in respect of industrial employees, they are far more restricted in the case of non-industrial employees. More generally, the ROFs are currently counted within the overall total of Civil Service numbers in spite of the fact that the Organisation's response to markets has long been accepted as the most appropriate criterion for its level of manning.

e. Powers to Fund the Purchase of Shares

Although the Secretary of State for Defence may purchase shares, the Government Trading Funds Act of 1973 does not permit ROF monies to be used to fund such purchases. The absence of the commercial flexibility to participate in joint company ventures or to take over other companies places the ROFs at a disadvantage at a time when there is an increasing trend towards collaborative projects, both nationally and internationally.

f. Export Credit Guarantee Department Facilities

These facilities, especially low interest credit, are necessary ingredients of some export deals. But one Department of State cannot guarantee another; so the credit and insurance cover available to commercial exporting organisations is not available to the ROFs.

g. Public Sector Constraints

There are a number of constraints which apply to the ROF Trading Fund simply because it is in the public sector. As noted above, its employees are Civil Servants; borrowing is a charge against the PSBR; and the fact that commercial decisions are open to E&AD and Public Accounts Committee scrutiny could be argued to have a generally

depressive effect on commercial activity. Though conversely there is the evidence of the considerable amount of ROF speculative work which has taken place in the past few years.

OPTIONS FOR CHANGE

11. Against the background of these constraints, we are convinced of the need for change. This view has been endorsed by the ROF management, by the British Army as customer and by the Ministry of Defence. Similarly both the Staff Side and Trade Unions representing ROF employees submitted papers to us in which they recognised the need for change, although they felt that this should take place exclusively within the framework of the Government service. In assessing the various options for change, we have identified a number of criteria against which they should be judged. These criteria are:-

- a. Does the solution improve the effectiveness of the Royal Ordnance Factories in meeting the requirements of the United Kingdom Armed Forces.
- b. Does the option involve the most efficient use of national resources.
- c. To what degree does the option remove or alleviate constraints on pay and manpower arising from the imposition of standard Civil Service arrangements.
- d. To what degree does the option remove or alleviate constraints on design and development and on marketing and sales to create a fully commercial entity.
- e. To what degree does the option remove or alleviate the constraints on access to ECGD facilities and on the formation of links with private companies.
- f. Does the option lead to any reduction in public expenditure.
- g. Does the option lead to any reduction in the total number of Civil Servants.

In addition to the above we are also agreed that it is desirable that whatever solution is eventually chosen should be broadly acceptable to the ROFs workforce.

12. With these considerations in mind we identified a number of options for the future development of the ROFs which are as follows:-

The Evolved Trading Fund

I. The ROFs would remain as a Trading Fund organisation but certain measures could be taken to ameliorate the constraints identified in paragraph 10. a. to g. In essence these measures would be as follows:-

a. The ROFs would be given their own sales arm and it would appear that this objective is achievable in the short term by the transfer of functions currently exercised by the Defence Sales Support Division of the Defence Sales Organisation.

b. The ROFs would be given responsibility for the balance of the contractual work associated with ROF products.

c. In line with the recommendations of the review of the R&D Establishments the ROFs would take on more design and development work.

d. In the personnel field the ROFs would need to have greater control over the conditions and service of their staff, in particular their non-industrial staff. (The Mallabar Report visualised a special ROF group within the Civil Service).

e. An amendment to the Government Trading Funds Act of 1973 could be made to allow the ROFs to purchase shares and become involved as a risk sharing partner both in consortium deals and manufacturing operations at home and abroad.

f. Legislation could be enacted deeming the ROFs not to be a Crown service so that the Organisation could have access to both ECGD cover and credit.

Disposal to Private Industry

II. The assets of the ROFs could be sold off to private buyers on a factory by factory basis or in functional groups or the Organisation could be sold off in its entirety.

Creation of a Companies Act Structure

III. The ROF Organisation could be given a Companies Act structure 100% Government owned. Subsequently it could either:-

a. itself move into private ownership through the sale of shares and relinquishment of Government control;

or

b. create subsidiary companies, each responsible for a part of the Organisation some or all of which would move into private ownership through the sale of shares.

Nationalisation

IV. The ROF Organisation could be turned into a nationalised corporation.

Creation of Agency Factories

V. The ROF Organisation could be turned into a group of Agency Factories run along the lines of the two Agency Factories, Powfoot and Featherstone, already in existence.

GENERAL CONSIDERATIONS

13. The present ROF Organisation came into being as a result of a statutory instrument under the Government Trading Funds Act of 1973. Any move to change its status significantly eg Option III would require major legislation. With the possible exception of Option IV, none of the other options would involve anything other than minor legislation.

14. We recognise that the costs and benefits of the various solutions would need to be rather more clearly defined. We are aware that the Organisation's market value at present would be depressed because business had fallen off sharply as a result of successive severe blows from the loss of major Iranian orders (which subsequent export orders have not offset), an industrial dispute, and a reduction in orders from the Services. We are also aware that any proposal to move Civil Servants to the Private Sector would involve questions of redundancy compensation, pension rights, transfer values etc which would need to be set against any financial benefits accruing from disposal.

15. The attitude of the workforce to any solution involving a degree of privatisation is likely to be, initially at least, unfavourable.

DISCUSSION

16. There is no support for nationalising the Organisation in its entirety (Option IV) nor for the option of turning the ROF into Agency Factories (Option V).

17. In considering the three remaining options, the study group regarded the following points of principle as relevant:

a. If it is accepted that the trading fund would only be an interim stage of development, it could be argued that a move to privatisation should involve the organisation in its entirety. Among the reasons for privatisation as an entity is that the organisation is structured as an inter-dependent body and that the flexibility in operation which this structure gives is an argument against any degree of fragmentation.

b. On the other hand, there are arguments for considering the privatisation of the ROF organisation in parts, either by selling off (Option II) or under the umbrella of a Companies Act Holding Company (Option IIIb). The benefit in the 'selling off' approach is seen to be that, in the Option III case, this would be the best way of exposing the organisation to market forces and that in the Option II case, this would provide a less complicated solution.

18. On the question of timing, the study group consider that it would probably take at least two years for the organisation's financial position to improve and it would also take some time to enact any major legislation which might be required. But for most of the options some interim steps could be taken straight away.

CONCLUSIONS

19. We all recognise the success which the Royal Ordnance Factories Organisation has achieved since the setting up of the Trading Fund in 1974. Similarly we recognise the need for some change given the constraints which have been identified and the fact that the trading environment both at home and abroad has changed dramatically in the past two years.

20. We conclude that there are three main Options open for future development:

a. To improve the present Trading Fund Organisation by removing some of the impediments which we identified (Option I).

b. To dispose of the Organisation to the Private Sector either as a whole or in parts (Option II).

c. To turn the Organisation into a Companies Act structure in its own right and involve private capital by flotation of shares of itself or of subsidiary companies (Option III).

21. We recognise that the Options are not exclusive and that it would be possible to move to Option II via Options I and III.

STUDY INTO THE STATUS OF THE ROFsTerms of Reference

"The Study should consider all possible lines of future development for the ROF Organisation, in particular the scope for privatisation, and should recommend whether one, or more, of these should be adopted in preference to continuation as a Trading Fund".

Composition of the Study Group

Chairman	Minister of State, Ministry of Defence
Two ROF Members	W Meakin Managing Director J E Carruthers Director of Finance
Two Members from Ministry of Defence	Maj Gen J A Stephenson Deputy Master General of Ordnance Mr R Anderson Deputy Under Secretary of State (Procurement Management and Sales)
A Treasury Representative	Mr Hansford Assistant Under Secretary of State
Two Department of Industry Representatives	Mr David Young, one of Sir Keith Joseph's Special Advisers and Mr John McEnery Assistant Under Secretary of State
Three outside Members	Sir Charles Ball - formerly with Barclays Merchant Bank Dr Adolf Frankel - Staveley Industries Limited Mr Brian Jenkins - Coopers & Lybrand, longest serving outside Member of the ROF Board

The ROF Board Secretary, Mr McLoughlin, was
Secretary to the Study Group

THE ROF TRADING FUND

The Royal Ordnance Factories Trading Fund Order 1974 followed from the Government Trading Funds Act of 1973 and on 1 July 1974 the operations of the Royal Ordnance Factories ceased to be financed by means of annual Votes and appropriations and were instead to be financed by a Trading Fund.

Trading Fund operations require that the ROFs buy and sell goods and services in a commercial manner and the ROFs operate to a financial objective agreed by the Ministry of Defence and the Treasury. The Managing Director Royal Ordnance Factories is the Accounting Officer for the Trading Fund and answers to Parliament through the Public Accounts Committee for his management of the Trading Fund.

The Order defines the operations to be financed by the Fund as:

(a) The supply of any article intended or adapted for use by the Armed Services of the Crown, or the Armed Services of the Government of any other country or of any international organisation.

(b) Any operation incidental or conducive to the conduct of the operations described in paragraph (a) including the supply to any person, Government or international organisation of any article which may be conveniently supplied in conjunction with those operations.

"Supply" includes manufacture, processing and equipping and any associated research or development work.

THE ROF BOARD - TERMS OF REFERENCE

"Under the general policy direction of the Minister of State for Defence the Board of the Royal Ordnance Factories will consider matters of ROF policy and planning relating to the factories under the control of the Managing Director Royal Ordnance Factories. The Board will provide the forum for discussion on these matters and be the source of advice and support needed to enable the Managing Director effectively to discharge his responsibilities."

COMPOSITION OF THE ROF BOARD

Chairman:	The Viscount Trenchard	Minister of State for Defence
Deputy Chairman:	Mr W Meakin	Managing Director Royal Ordnance Factories

Full-Time Executive Members

Mr H Pointon	Director General of Weapons and Fighting Vehicles
Mr H Butterworth	Director General Ammunition
Mr J E Carruthers	Director General of Finance and Procurement

Part-Time Membersi. From the Ministry of Defence

Sir Ronald Ellis	Head of Defence Sales
Maj Gen J A Stephenson	Deputy Master General of the Ordnance
Mr I H Johnston	Deputy Controller of Establishments

ii. From Outside the Ministry of Defence

Mr B G Jenkins	Messrs Coopers & Lybrand, Chartered Accountants
Mr E J Challis	Formerly with ICI Ltd
One Post Vacant.	

Secretary: Mr T P McLoughlin, Director of Ordnance Factories
Plans & Secretariat

DETAILS OF FACTORIES IN ROF ORGANISATION
AND THEIR MAIN ACTIVITIES

<u>Factory</u>	<u>Main Activities</u>
ROF Birtley Co Durham	Equipped for design, development and mass production of wide range of brass and steel cartridge cases, armour-piercing shot, shell cases and rocket motor tubes.
ROF Bishopton Renfrewshire	The UK's largest producer of propellants for use in gun ammunition, rockets and guided weapons. The sole UK manufacturer of combustible charge containers.
ROF Blackburn Lancs	Designs, develops and produces fuzes, guided weapon safety and arming units, infantry and tank targets and a wide variety of electronic equipments.
ROF Bridgwater Somerset	The main factory for the manufacture of military high explosives in the UK. Also the principal factory for manufacture of plastic propellants and their filling into military and civil rockets.
ROF Chorley Lancs	Fills all types of munitions ranging from grenades, through mines to heavy calibre artillery ammunition.
Royal Small Arms Factory Enfield Middlesex	One of the leading manufacturers of small arms in the world, capable of designing, developing, manufacturing and testing complete products ranging from personal infantry weapons to 30mm calibre cannon.
MOD Agency Factory Featherstone (Wimet Ltd) West Midlands	Manufactures hard metal components of high density for use in armour-piercing projectiles.

FactoryMain Activities

ROF Glascoed
Gwent

Its prime function is the assembly and filling of gun ammunition, mines, bombs, rockets and grenades with propellants, explosives and smoke composition and explosives substitutes. Particular expertise in smoke generating and chemical defence work.

ROF Leeds
Yorkshire

A heavy engineering factory with a full range of facilities for the manufacture of armoured fighting vehicles in steel or aluminium alloy and their associated equipments. The principal UK source of Main Battle Tanks; also provides logistic and post-sales support services.

ROF Nottingham

The principal factory for the development and manufacture of guns and mountings, mortars, rocket launchers, engineer equipment and special vehicles.

ROF Patricroft
Nr. Manchester

Equipped to produce bombs and projectiles, shells, missile warheads, heat-resistant plastics, rocket motors and aircraft rocket heads.

MOD Factory Powfoot
(Nobel's Explosive co Ltd)
Dumfries

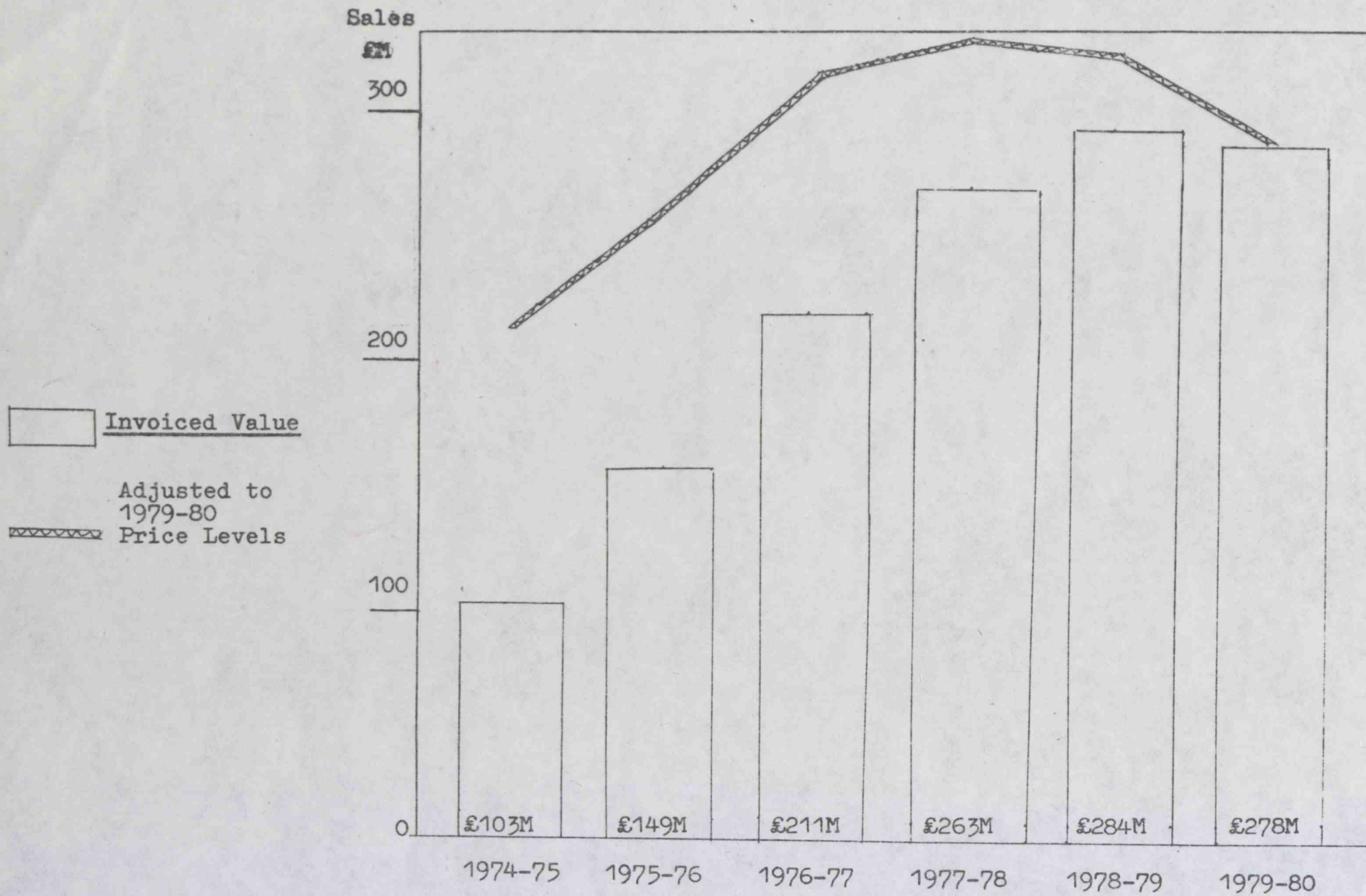
The only UK source of single base propellants. The main products are rifle and cannon powders.

ROF Radway Green
Nr. Crewe
Cheshire

Manufacture of small arms ammunition.

[ROF Consultancy and
Advisory Service, Leeds

Established to supply technical advice, usually in conjunction with a Licence Agreement, on all aspects of manufacture undertaken in the ROFs. Offers a comprehensive service which ranges from technical advice on a consultancy basis to the provision of detailed engineering plans.]



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9 JUN 1901

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Prime Minister

MP 462

C. M. Lyhan



MO 10/4

The report at Play A is to be put in the House Library tomorrow. It canvasses 3 main options, without coming down in favour of any one in particular.

Mr. Mott is proposing something on the lines of (c), which he would announce in his defence

CHANCELLOR OF THE EXCHEQUER

THE ROYAL ORDNANCE FACTORIES

statement. This looks the best way forward, but I suggest you leave this to him and the Chancellor.

I recently received the report of the Study Group. It could not agree on the way forward but outlined three possibilities:-

a. development of the ROF organisation within the Trading Fund concept, particularly to acquire its own sales force and design and development capability, and to have greater control over the conditions of service of its staff.

D. 4/6

b. Sale in whole or in parts to private industry.

c. A change of status to that of a Companies Act Company (or several such companies) with the equity initially held 100% by Government but with the idea of flotation of some or all of the shares at a later stage.

2. The ROF's have been part of Government since before the 1914-18 war, some parts for very much longer. The Mallabar (1968) and Rayner (1971) Reports both recommended that the ROFs remain within the MOD but these reviews led to the creation in 1974 of the present Trading Fund. Until 1979/80, the performance of the organisation had been creditable, but with the loss of the Iran orders and a falling off of business generally, the Study Group considered that it would probably take at least 2 years for the organisation's financial position to improve. The present is thus not a good time to sell - the net asset value is about £150m



and while we have some independent advice that such a sum would be realised as a minimum, a higher value could be expected if business improves. On the other hand, redundancy costs would have to be met if we proceeded down course (b), as well as the transfer value of accrued pension rights. Both could have significant public expenditure implications probably exceeding £150M in total, (though, as the pension rights are already liabilities, it would be right, I understand, for these to be ignored in cost comparisons).

3. Moreover confidential exploratory soundings suggest that no one industrial firm will buy all the ROFs; and in discussions about the sale of most of the factories to 3 separate organisations, the reaction remains cautious and is likely to be so until substantive negotiations against a firm MOD order book can be initiated. Even then, the financial problem of the size of likely receipts from sale in present circumstances would remain.

4. We could decide on course (a), which need not exclude privatisation later when the financial prospects might be better. I do not recommend this. I believe that there is no reason in principle why this part of defence industry rather than any other should be in Government ownership; the task of recruiting a sales force and turning a production enterprise into a fully fledged commercial organisation is not one which Ministers and their advisers are well equipped to perform, and it would be consistent with our policy of reducing the size of the public sector to decide now to move towards some form of privatisation. This brings me to course (c).

5. There are arguments for and against keeping the organisation as a single unit (a situation strongly favoured by the present management). The complex personnel problems would certainly be



more manageable if this were the chosen route. But I believe that provided we did not have more than 3 groups, or at most 4, (and the organisation falls naturally into such groupings) such problems should be containable.

6. An early statement of Government policy is needed. There is much speculation at the factories and in Parliament; and uncertainty will also have its effect on present and potential customers. For the reasons given, I believe that while not abandoning the possibility of selling off one or more of the factories if an acceptable deal can be struck we should make course (c) the main thrust of our policy. We should now seek legislative powers accordingly. Prudently these would allow us to form a single or a number of Companies Act companies, the precise decision to be taken later. But, while the powers would be general, my present preference is for a solution on the following lines:

a. a marriage between groups of factories (eg armoured vehicles; guns and ammunition; fuzes; explosive materials) and the relevant parts of industry, (such as Vickers, Guest Keen, Thorn/EMI and ICI) achieved by the creation of Companies Act companies in which:

(1) the equity is shared - initially at least - between the Government and the relevant firm(s) in agreed proportions.

(2) the manning of the management and the commercial and financial administration of the new joint companies would be overhauled. The private sector partner as well as providing commercial expertise would also contribute the sales know-how which the ROFs do not now possess.



b. these new joint companies would have the appropriate R&D capabilities which, for the most part, lie at present in the MOD's own R & D Establishment, the ROFs being largely a production organisation only. Incorporation of MVEE (Chobham) and PERME (Waltham Abbey) will be an objective; certain capabilities at RARDE (Fort Halstead) may also have to be transferred to the new companies.

7. I would hope that the whole process of legislation, identifying industrial partners for cohesive groups of factories, the creation of the new joint companies with the associated R&D capabilities, the appointment of initial management (in which we would have to have a say), and the necessary staff consultations could all be completed by 1st April 1983. As with course (b), a short term public expenditure problem can be expected for pension transfer values and redundancy payments, but the extent of these cannot be estimated until we are aware of the terms of service which the new joint companies would offer and the likely preference of the staff themselves. But such transitional costs must be faced as part of our privatisation policy generally.

8. If you and the Lord President agree, I should like to make a statement in general terms on these lines as part of the more general statement I expect to make to Parliament early next month about the defence programme as a whole. This will enable us to move forward more openly with the staff and with potentially interested parts of industry than has been possible so far; and to do so in a direction consistent with our general policies as a Government. If industry fails to co-operate, we will have to think again; but in such circumstances the omens for a flotation of shares, as with BAe, would not seem good.



9. Finally, there is the question of the effect on the defence budget of the change: for example we can expect to pay more since the ROFs would be entitled to contracts governed by the profit formula.

10. I am sending copies of this minute to the Prime Minister, the Home Secretary, the Secretary of State for Industry, the Chancellor of the Duchy of Lancaster, the Lord President, the Chief Secretary; and Sir Robert Armstrong.

SW

Ministry of Defence

5th June 1981

Gorb Mach.



✓
MA

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

26th February 1981

B.M. Norbury Esq.
Private Secretary
Ministry of Defence

Dear Brian,

FUTURE OF AWRE AND THE NUCLEAR ROFs

Thank you for copying to me your letter of 16 February 1981 to Julian West on the future of AWRE and the nuclear ROFs.

The Chancellor has seen the study of the arguments for change from a defence point of view which you attached to your letter, and agrees with your Secretary of State that the question of changing the status of AWRE and the nuclear ROFs should not be pursued further.

I am sending copies of this letter to the other recipients of yours.

Yours sincerely

John Wiggins

A.J. WIGGINS
Private Secretary

27 FEB 1981





Good Mad

10 DOWNING STREET

Clive ^{then} ^{of} ^{Mad} ¹⁶⁻¹¹

We did not trouble the
PM with the proposition
below; so need not
tell her that it has
been dropped. But
you may like to see.

MAD
16/12.

great Mad

CONFIDENTIAL



MINISTRY OF DEFENCE

MAIN BUILDING WHITEHALL LONDON SW1

Telephone 0 ~~300 7022~~ 218 2111/3

MO 20/17/7

16th February 1981

*N&N.**KW**16th**Dear Julian,*FUTURE OF AWRE AND THE NUCLEAR ROFs

Since my then Secretary of State wrote to yours on 22nd September last year proposing an examination whether the Atomic Weapon Research Establishment (AWRE) and the two nuclear Royal Ordnance Factories, ROF Burghfield and ROF Cardiff, should be transferred to the Atomic Energy Authority (AEA) our officials have been in touch and an informal Study Group has considered the arguments for change from a defence point of view. In addition to transfer to the AEA, the Study Group looked at two further options: the creation of a publicly owned nuclear weapons company and the transfer of the defence nuclear R&D and production organisation to private industry. I attach a note setting out the conclusions reached by the Study Group (which concentrate particularly on the control issues which lay behind the 1973 Act).

My Secretary of State has considered the report of the Study Group in the light of the reservations expressed earlier by your Secretary of State and the Lord President, and in the light of the facts that the re-organisation of civil nuclear work since 1973 has changed the character of the AEA so that it would be difficult to revert precisely to the same arrangements, and that experience has shown that there are considerable benefits to be gained from maintaining the closest possible coherence of nuclear warhead development and production and that it would, therefore, be undesirable for the work carried out at AWRE to be conducted under a separate authority from that at the nuclear ROFs (before 1973, the AEA had no responsibility for the production of nuclear weapons and thus lacks experience in this field).

J D West Esq

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MANAGEMENT IN CONFIDENCE

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While the same considerations do not apply in the case of a publicly owned nuclear weapons company formed out of AWRE and the nuclear ROFs, it is questionable whether this concept would prove more efficient or economic than the present arrangements, and it would do nothing to alter the balance between the public and private sector. In this respect, the private nuclear weapons company offers a more attractive alternative but it carries a serious risk of disruption to the Trident programme; presents the greatest political difficulty at a time of increasing controversy about civil and defence nuclear programmes; and would represent an even greater change of direction in the handling of these affairs than returning to the situation before the 1973 Act, not least because production of nuclear weapons has always been under the direct control of a Minister. Nor is the product marketable other than to HMG.

Under these circumstances and after careful consideration of the issues, my Secretary of State has concluded that the question of changing the status of AWRE and the nuclear ROFs should not be pursued further.

I am sending copies of this letter to Clive Whitmore (No 10), George Walden (FCO), John Wiggins (HM Treasury), Jim Buckley (CSD) and David Wright (Cabinet Office).

Yours ever,
Brian Norbury

(B M NORBURY)

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CONCLUSIONS OF MOD STUDY ON THE FUTURE OF AWRE AND THE
NUCLEAR ROFs

1. The MOD study considered three broad options for the transfer of AWRE and the nuclear ROFs: transfer to the UKAEA, the creation of a publicly owned nuclear weapons company and the setting up of a private nuclear weapons company. The conclusions reached by the study on each option are summarised in paragraph 2-4; since the civilian manpower implications are broadly the same under each option, they are summarised in paragraph 5.

2. UKAEA 'Weapon Group'

This concept appears to offer few advantages by comparison with the present arrangements or indeed with the alternative options for change. While it should be possible to ensure through legislation that the MOD retained broad policy control, there would inevitably be some weakening of the Department's ability to direct policy within AWRE and the nuclear ROFs. Similarly, whilst it should be possible to adjust the programmes to meet changing budgetary or political programmes, it is unlikely that changes could be made as quickly or easily as at present. Although it is not possible to be categorical at this stage, efficiency would not necessarily be improved and could be adversely affected because of UKAEA's lack of experience appropriate to the current MOD programme and the weakening of MOD control. This could affect the efficient management of current programmes for some time, while in the short term disruption would be unavoidable at a time when little disruption could be tolerated. The UKAEA 'Weapons Group' would be likely to cost just as much as the present arrangements and could be more expensive; although it is difficult to quantify costs there are certainly no grounds for assuming savings would be made. Finally, the Secretary of State for Energy has pointed to the presentational problems in associating the civil and military nuclear programmes at a time of considerable public interest in and debate about both.

3. Publicly Owned 'Nuclear Weapons Company'

Under this option, there could be a gain in the amount of flexibility which could be granted to management to deal with specific problems but there would also be a number of significant disadvantages by comparison with present arrangements. As in the case of the 'Weapons Group', the MOD could retain a degree of broad control over policy through both the constitutional arrangements for the Company and as a consequence of the Department's financial control, but this would be less than at present. Similarly, while the MOD would be able to regulate the programme to take account of changing considerations, the scope for doing this would be reduced. While an increase in management flexibility should in theory improve the prospect of programmes being completed within the planned timescales, in practice change is bound to be disruptive and this could lead to some slippage in the currently established programme in the short term. This could in turn affect the timescale for the completion of the programme in the long term, although enhanced efficiency might enable some lost time to be made up. It seems likely that in the short term there would be some additional costs to the defence budget but the scale of this cannot be judged with any certainty. Greater efficiency could produce savings in the long term, but there can be no assurance of this. The potential political and presentational difficulties of associating the civil and military nuclear programmes under one authority, the UKAEA, would not arise, but there would still be a potential presentational problem in that the completed deliverable nuclear weapon would be produced by and temporarily the responsibility of, an organisation other than the Ministry of Defence:

4. Private Nuclear Weapons Company

The conclusions summarised at sub-para (b) relating to a publicly owned 'Nuclear Weapons Company' are also in the main valid in the case of the private Company although the potential advantages would be greater and the disadvantages more acute. Management could enjoy much greater flexibility than at present, depending on the extent to which the Company was divorced from Government control, but the weakening of MOD control over policy direction would also be correspondingly greater. The regulation of resources in the Defence Nuclear Programme to meet changing political or budgetary circumstances could be less effective; short term costs would be likely to increase but, in the longer term savings might accrue from higher efficiency. The creation of a private Nuclear Weapons Company would however involve the greatest political difficulties of all the options and these difficulties would apply not only to the Government but also affect any private industrial concern which could be found willing to assume responsibility for nuclear weapon development and production. This solution would also bring the greatest risk of disruption at the transitional stage

5. Civilian Manpower

The Ministry of Defence is required to make very substantial reductions in its civilian staff manpower and the transfer outside of MOD of 6000 staff, would, if acceptable (as seems possible) as a reduction in Civil Service numbers, make a significant contribution to meeting the Department's target. Moreover, it would obviate the need for further manpower increases in the Defence Nuclear Programme as work on the currently approved programme builds up. This transfer of staff could be accomplished under any of the options above. Under none of the options, however, would short term savings be expected to accrue to the Department as a result, since staff would have to be offered acceptable conditions of service in the new organisation and the costs would be reflected in the prices charged to MOD. The Department could face difficulties should it ever prove necessary to reabsorb the transferred staff. Because the Department and the new organisation would be dealing with each other as separate entities some increases in staff would be necessary in both, although within MOD there should be some marginal staff reductions in existing functions. The benefits of transferring staff would thus be presentational rather than substantial.

THE FUTURE OF AWRE: ADVANTAGE AND DISADVANTAGES OF CHANGE

INTRODUCTION

1. Following Ministerial correspondence, it was decided to prepare a report setting out more fully the arguments from the defence point of view for change. This note identifies the options and considers these in relation to the criteria which would be central in evaluating the advantages and disadvantages of change in the status of the Defence Nuclear Organisation.

THE OPTIONS

2. Broadly there are three options to be considered for the management structure for the Defence Nuclear Programme (DNP):

(a) a continuation of the existing arrangement under which the DNP is run on an integrated basis wholly within MOD;

(b) a transfer of AWRE and the nuclear ROFs to an existing public body, ie the UK Atomic Energy Authority (UKAEA) (for ease of reference, this is hereafter called the "Weapons Group" option);

(c) the establishment of a new organisation separate from any existing public authority. Under this option, AWRE and the nuclear ROFs could be hived off either

- (i) in a manner similar to that adopted when British Nuclear Fuels Ltd (BNFL) and The Radiochemical Centre Ltd (TRCL) were created to form independent entities within the public sector or
- (ii) to form a component of an existing private company.

This option is referred to hereafter as the "Nuclear Weapons Company" option and, where necessary, the sub-options are identified as "public" and "private" respectively.

Since this paper is concerned primarily with the options for change, (a) above is not considered directly in the analysis. Nonetheless, it must be recognised that the present organisation provides the yardstick against which the other options are judged.

3. Options (b) and (c) do not allow for the separation of AWRE and the nuclear ROFs at Burghfield and Cardiff. Although before 1973, nuclear R & D was managed separately from production, recent experience (in particular of the Chevaline project) has demonstrated that the pattern of development and production in modern programmes is very different from that in earlier programmes. It is expected that in the Trident programme, as with Chevaline, development and production will dovetail to the extent that the two may be indistinguishable at some stages. It is thus vital to ensure that

the greatest coherence of development and production is preserved if the full requirements of programmes are to be met. This paper therefore assumes that any change would embrace both AWRE and the nuclear ROFs. This could, however, carry a potential political penalty: the reason for the separation of the production and development organisations between 1954 and 1973 was the perceived need to ensure that the final product, the deliverable nuclear weapon, remained under the control of a Government Minister and his Department. Hiving off the production organisation would mean that an organisation other than a Government Department would produce and temporarily have possession of the completed nuclear weapon.

4. The implications of change would depend to a certain extent on the type of new organisation envisaged. It is therefore worth considering briefly how each might operate. The return of AWRE to UKAEA would require the setting up within the latter organisation of a new 'Weapons Group' which would be administered by the Authority, although it could on past experience enjoy a fair degree of autonomy within that body. Under the 1954 Atomic Energy Authority Act, Ministerial control of UKAEA was vested initially in the Lord President of the Council, and now in the Secretary of State for Energy, although he is not empowered to intervene in its detailed affairs except in the event of overriding national interest. A 'Weapons Group' within UKAEA would thus be constitutionally separate from MOD and compensating arrangements to enable the Secretary of State for Defence to exercise a degree of control would need to be provided for in the enabling legislation, on the lines which existed before 1973. Provision would also be needed for consultation between the Secretaries of State for Defence and Energy in the event of a conflict of priorities.

5. The public Nuclear Weapons Company concept is one under which the MOD would set up an autonomous organisation, separate from the Department, owned by HMG (possibly by the Secretary of State for Defence), and accountable to the Secretary of State for Defence. The Company would take its policy direction from MOD, through a Board of Directors, of which the Chairman and possibly other members could be MOD officials, while commercial experience could be brought to the Board by the appointment of outside members.

6. Under the concept of a private Nuclear Weapons Company, responsibility for the management of AWRE and the nuclear ROFs would be transferred, under terms to be agreed, to an existing private commercial company. The company would be required to operate the facilities exclusively for nuclear weapons purposes unless otherwise agreed by MOD and the operations of the facilities would be financed by MOD contracts. As a minimum the company would be responsible for running the facilities, including the provision of staff. The extent to which the company would take over the assets of AWRE and the nuclear ROFs, and the responsibility for renewing them, would be a matter for negotiation.

7. In order to prevent massive disruption of the present defence nuclear programme, the staff of either new organisation would have to come very largely from those now working within the present

Defence Nuclear Organisation. This would entail persuading the staff concerned to transfer; for the transfer to be acceptable, pay and conditions of service would need to be offered which, taken as a whole, were not less favourable than those currently obtaining in the Civil Service.

THE CRITERIA

8. The main factors to be taken into account in assessing the options are:

- (a) would MOD's policy direction be strengthened or weakened?
- (b) would MOD be more or less able to regulate the programme to meet changing budgetary or political considerations?
- (c) would procurement and R & D be managed more or less efficiently; would management gain or lose flexibility to deal with special circumstances in production or staffing?
- (d) would the likelihood of achieving the currently-established programme be improved or lessened, both during any period of transition and in the longer term?
- (e) would the cost of meeting the defence nuclear programme increase or decrease?
- (f) what would be the effect on MOD civilian numbers?

These questions are closely interrelated and the following discussion identifies the main points which occur under each.

Strengthening or Weakening of MOD's Policy Direction

9. It seems indisputable that either option would entail some lessening of MOD control; the extent of this varies with each. The 'Weapons Group' would be under the authority of UKAEA, which would have responsibilities to two different Ministers of the Crown. Nonetheless as the sole customer of the 'Weapons Group', the Department could be expected to have substantial influence on the Group's policies and operations, the full extent being dependent on the enabling legislation. Equally just as the MOD as sole customer would influence the 'Weapons Group', the position of the Group as a monopoly supplier controlled by a body with its own research programme and interests could affect the scope of the nuclear warhead programme. To prevent this it could be necessary to enshrine in statute that the Group could only undertake research and produce weapons in response to direct MOD orders. The Department would thus retain the ability to direct in broad terms the policy of the 'Weapons Group'. This policy direction would however be exercised through a non-MOD agent.

10. The "Nuclear Weapons Company" would similarly be a monopoly supplier with a sole customer. Under the public sub-option, the Company would not form part of a different organisation but would be autonomous with MOD control exercised through the MOD Chairman of the

Board and by virtue of the Board's accountability to the Secretary of State. Under the private sub-option, the Company would be part of a larger organisation but it is envisaged that the parent company would primarily provide the management infra-structure and the management expertise with MOD exercising policy control principally by budgetary means. The legislation necessary for setting up either the public or private Nuclear Weapons Company would bear on the scope of the MOD control but this would clearly be less than under the present arrangements, the more so for the private company.

Regulation of the Programme to Meet Changing Budgetary or Political Considerations

11. The need to ensure closer MOD control over and regulation of the executive management of the nuclear weapons programme was a major consideration leading to the setting up of the present organisation in 1973. There is no doubt that this has been achieved and was a major advantage of the 1973 reorganisation - the present system is highly responsive to requirements for changes in the programme and can react to them quickly. Under either option for change, MOD direction would be confined to broad policy; the Department would not have executive control, nor would it have the flexibility which is given by the present system of financial control, where the Ministry of Defence itself can directly allocate resources to the best effect between one part of the programme and another. The greater the autonomy of the organisation in the case of the Nuclear Weapons Company, or the degree of UKAEA control under the Weapons Group option, the more difficult rapid regulation of the programme to meet urgent requirements could prove.
12. In the longer term, the cycle of the defence nuclear programme and changing political considerations can lead to fluctuations in the flow of work. For an organisation to remain viable it must be capable of accommodating such fluctuations; it needs to be able to shed staff when work runs down and to build staff up again when new projects are undertaken. It may be necessary for changes in staff levels to be implemented rapidly. Under the present arrangements, there is some scope for peaks and troughs in the nuclear programme to be absorbed because the nuclear organisation is an integral part of a much larger body, the MOD. Staff can be transferred between AWRE and the nuclear ROFs and other areas of the Department. Such transfers would not readily be possible with a hived-off organisation. The UKAEA might be able to accommodate some fluctuations in the loading of the 'Weapons Group', but the Authority is much smaller than the MOD and would have correspondingly less flexibility. In the case of a public Nuclear Weapons Company, it would be necessary to consider whether to make legislative provision for the Company to diversify its activities in the event of a reduced nuclear weapons programme. A private Nuclear Weapons Company would almost certainly require such flexibility. It is possible that, if the Company had diversified its programme, it would find it difficult to respond quickly to a subsequent increased demand for weapons work. Giving rights to the public Company to diversify its activities could raise political issues apart from those associated with nuclear weapons.

Flexibility and Efficient Management of Procurement and R&D

13. It is difficult to quantify efficiency, but broadly, efficient management might be equated to the provision of the right goods at the right time while maintaining acceptable quality and prices. At present, the need for the Defence Nuclear Organisation to follow the procedures applicable to decision-making in central government imposes penalties in flexibility and in time, which in turn lead to increased costs. If the nuclear organisation were hived off in such a way that its management could be given a greater degree of independence and flexibility in decision-making this should lead to increased efficiency. One important example is the ability to adjust individual rates of pay; this could lead to improved recruitment of particular groups of staff where shortages risk prejudicing the timescale for completion of programmes. Another significant area is investment in new capital facilities where more flexible and rapid decision-making would enable requirements to be met more quickly. Flexibility could, however, add to the costs of the programme. Unless accompanied by improved productivity, increases in pay lead to increases in costs which would be passed on to the customer - MOB. Similarly, the costs of capital investment would be reflected in the prices charged: if MOD was unable to impose restraint, those costs could be higher than at present. The degree of flexibility which could be granted a new organisation could in some respects probably be greater in the case of the public 'Nuclear Weapons Company' - and certainly in the case of the private Company - than in that of the UKAEA 'Weapons Group', since under the latter concept, pay and conditions of service would need to be consistent with those of other staff in the Authority - and by extension the public sector as a whole. Greater flexibility would however entail some increases in cost.

14. In considering efficient management of the programme, there are grounds for concern about the absence of appropriate experience in the UKAEA relevant to the materials and techniques used in nuclear warhead work. The UKAEA has considerably reduced in size and is now fundamentally a research-orientated organisation. The Authority does not currently have the kind of expertise which would enhance efficiency in meeting the demands of the Defence Nuclear programme and the setting up of BNFL and TRC has further limited the UKAEA's capability. These considerations would affect the contribution which the UKAEA 'Weapons Group' concept could make to improving efficiency in the management of the Defence Nuclear Organisation, especially on the production side. Further thought would be needed to determine whether closer association between civil and military work (if politically acceptable - see below) could lead to better use of resources by sharing overheads and expertise in eg safety matters.

15. The problem of expertise in nuclear weapons development and production should be much less in the public Nuclear Weapons Company provided that the present staff agreed to transfer. Similarly there should be no difficulties with the private Company if the wholesale transfer of staff could be arranged. The private Company could however face greater problems than the public Company if insufficient staff transferred from MOD since none of the potential parent companies is likely to have expertise, at management levels or at more junior levels, relevant to either the broad sweep of nuclear weapons technology or the more general nuclear materials and safety fields

but it would be able to bring its experience to bear on the production and management sides of the DNP. However, if this experience were deemed desirable for the public Company it could be supplied by coopting Board Members from outside industry. Equally, under present DNP arrangements, greater use could be made of outside management and production expertise by employing consultants more widely.

16. It may be argued that transferring AWRE and the nuclear ROFs the UKAEA would lead to enhanced efficiency by opening up the possibility of transfers between the Authority and the Defence Nuclear Organisation. This however is to misunderstand the nature of the various disciplines required for the nuclear warhead programme, which relies on expertise in such varied fields as conventional explosives, engineering, metallurgy and so on. Expertise in these fields can be brought to AWRE by staff transferring from other MOD Establishments into the nuclear field; this has proved extremely valuable while the other Establishments have gained from the reverse flow. As has already been noted, UKAEA is largely lacking the kind of experience necessary for the defence nuclear programme; it could not provide the diversity of skills and staff which would be needed. Although some system of secondment from MOD might be possible under either of the options being considered, the practical results of such a scheme would probably be only minimal. The nuclear organisation could become more rather than less inbred.

17. It thus appears unlikely that the UKAEA 'Weapons Group' option offers any advantages in efficiency by comparison with the present organisation and indeed it could prove disadvantageous. In the case of the 'Nuclear Weapons Company' there are grounds for considering that the greater flexibility in day to day decision-making and in the margins of salary scales could lead to greater facility to meet the programme within the required timescale. The programme would probably prove more expensive than at present, but this needs to be set against the possibility that savings could be made by reducing the risk of delays in projects.

The Likelihood of Achieving the Current Programme During Transition Period and Thereafter

18. Since what is envisaged under either option is the wholesale transfer of staff from the MOD to a new body, in theory there should be no long term disruption. In practice, however, it is uncertain how far this wholesale transfer could be achieved. Even if offered pay comparable to or better than Civil Service rates, some staff might be reluctant to put at risk their present job security and career prospects in a politically uncertain field. This might be overcome, although the precedent would be an awkward one, by giving staff transferring reserved rights at least for a period to return to the Civil Service in the event of their posts being abolished (which would present the MOD with a serious management problem if large numbers had to be reabsorbed and would undermine the value of any reorganisation. Differential pay rates could also pose difficulties in these circumstances). This would, however, diminish the benefits of the new organisation's flexibility to 'hire and fire'. Provided staff are willing to transfer, there is no reason to assume that a new organisation would be unable to achieve the current programme in the long term.

19. The short-term implications of change are more open to question. The Chevaline and Trident programmes are at a crucial stage and there is no scope for delay or disruption. It is arguable that since most of the present workforce would be continuing their present task in the same place, even short term disruption would be minimal, but this ignores the effects of change on management. First, planning and organising change would inevitably occupy senior officials' time, diverting it from the management of the programme. Secondly, change to either option would involve changes in the structure of the management organisation, especially in the case of the Company where new people, lacking immediate experience of the programme would be brought into management. Moreover, it seems prima facie unlikely that under a new management structure there would be no attempts to change the way the programme was being run. While these might increase efficiency in the long run, in the short term any change is bound by its nature to cause a degree of disruption. This could lead to slippages in the current programmes.

The Cost of Meeting the Defence Nuclear Programme

20. Reference has already been made to the likelihood of salary increases leading to higher costs in the Defence Nuclear Programme unless the MOD exercised tight control and achieved offsetting savings through enhanced efficiency. The Department's position as customer of a monopoly supplier suggests a risk of higher prices. One further element which could raise costs is the introduction of a new tier of administrative staff (discussed in more detail below). In the case of a public Nuclear Weapons Company, further costs to MOD could arise through the Treasury setting financial targets to include a return sufficient to cover the costs of replacing existing capital assets. The private Company would certainly make charges for this purpose. Consequently, the Company would have to include a profit element in the prices charged to the Department. It is not clear whether this increase in costs would be fully-off-set by the savings to MOD from being relieved of the responsibilities for direct funding of new capital projects, but it seems likely that the trend would be towards some increase by the cost of the Defence Nuclear Programme.

Effects on Civilian Manpower

21. Within MOD over 6,000 people are employed at AWRE and the nuclear ROFs. This number is expected to rise to over 7,000 by 1984. The Department is required to reduce its civilian staff by over 30,000 between now and 1.4.84. Given the reductions in civilian manpower which have been made in the past decade, it will be difficult to find cuts of this order without prejudicing the defence programme and defence operations. Against this background a reduction in civilian numbers of the order which could be achieved by hiving off the Defence Nuclear Organisation would clearly be significant. It appears that a reduction in Defence manpower achieved in this way would be acceptable as part of MOD's effort to meet its target.

22. If the Defence Nuclear Organisation were hived off, some increases in administrative staff would be necessary, both within MOD and the new organisation. As far as MOD is concerned, the scale of increase would depend on the relationship between the two bodies; project management and contracts staff might be required and it would be necessary to provide for some system of financial control and auditing. Marginal reductions should be possible in the number of MOD staff currently involved in some functions dealing with the Defence Nuclear Organisation in Civilian Management, in CER's area and elsewhere. If the new organisation took the form of a UKAEA 'Weapons Group' it might prove possible to provide some administrative effort from within the Authority, although experience before 1973 suggests that separate administrative hierarchies are more likely. In the event that a 'Nuclear Weapons Company' was formed, extra staff would almost certainly be required.

Presentational Factors

23. In considering the advantages and disadvantages of change, four further factors relating to presentation will need to be taken into account. First, any change would need, as indicated by the Lord President, to be reconciled with the arguments deployed to justify the 1973 take-over of AWRE from AEA: that since the great bulk of AWRE's work was defence-related, the Establishment should come under the control of the Ministry of Defence and within the scope of the newly created Procurement Executive, and that this would enable considerable rationalisation between R & D Establishments. (In particular, R & D on conventional explosives was intended to be transferred to Aldermaston). The objective of strengthening MOD control over nuclear warhead R & D has clearly been achieved; the management of AWRE is fully integrated within the MOD. Moreover, the proportion of AWRE's work arising from defence requirements has risen from 75% to 97%. The second objective, the rationalisation of the facilities and resources of the R & D Establishments, has not been implemented to any significant extent. In particular, work on explosives for conventional weapons has remained distinct from that on conventional explosives for nuclear weapons, in part because of fears that if the two were brought together under one Establishment, conventional programmes would suffer as a result of the priority given to the nuclear work. Both options for change pose the problem however of explaining what would in essence be a reversal of the 1973 decision to increase the extent and closeness of MOD control over the development of nuclear weapons - and indeed the 1953 decision that their production should remain the responsibility of a central Government Department. It would be difficult to avoid the implication that these decisions had been mistaken and the MOD was not capable of carrying out its role efficiently.

24. The second factor which would need to be taken into account relates to public interest in and concern about nuclear weapons. Nuclear matters are currently the focus of considerable public attention; it would be important to avoid implying that the present nuclear programme was not being properly managed and controlled, or alternatively that it would be under less stringent Government control in the future. There is currently a clear separation between the civil and military nuclear programmes; bringing these programmes together would lead to increased suspicion of the civil nuclear programme and this in turn would be likely to rebound on the defence programme.

25. Thirdly, as recently as last autumn, MOD procurement arrangements in the nuclear warhead field were reviewed and changes made, resulting in the creation of the post of DCDP(N) with overall responsibilities for nuclear R & D and production.

26. Finally, while the Weapons Group or the public Nuclear Weapons Company options could be implemented by Government decision, subject only to constitutional processes, the private Nuclear Weapons Company option could be realised only with the cooperation of a suitable existing commercial organisation. It has not been possible to identify an organisation which would be both willing and competent to undertake the tasks. Even if an existing Company could be found, there must be doubts about the political acceptability of this option, despite the fact that it most closely corresponds in principle to the current US organisation for their DNP (see Annex). Public opinion would probably react strongly against the concept of allowing private industry to have apparent control over nuclear weapons and those industrial organisations which might be technically capable of undertaking the DNP would probably be at least reluctant, if not actively opposed, to assuming responsibility for a politically controversial element of the defence programme.

Conclusions

27. The conclusions which can be drawn on each option are summarised and (a), (b) and (c) below. Since the implications for civilian manpower are broadly the same under each option, the latter are summarised at (d):

(a) UKAEA 'Weapons Group'

This concept appears to offer few advantages by comparison with the present arrangements or indeed with the alternative options for change. While it should be possible to ensure through legislation that the MOD retained broad policy control, there would inevitably be some weakening of the Department's ability to direct policy within AWRE and the nuclear ROFs. Similarly, whilst it should be possible to adjust the programmes to meet changing budgetary or political programmes, it is unlikely that changes could be made as quickly or easily as at present. Although it is not possible to be categorical at this stage, efficiency would not necessarily be improved and could be adversely affected because of UKAEA's lack of experience appropriate to the current MOD programme and the weakening of MOD control: This could affect the efficient management of current programmes for some time, while in the short term disruption would be unavoidable at a time when little disruption could be tolerated. The UKAEA 'Weapons Group' would be likely to cost just as much as the present arrangements and could be more expensive; although it is difficult to quantify costs there are certainly no grounds for assuming savings would be made. Finally, the Secretary of State for Energy has pointed to the presentational problems in associating the civil and military nuclear programmes at a time of considerable public interest in and debate about both;

(b) Publicly Owned 'Nuclear Weapons Company'

Under this option, there could be a gain in the amount of flexibility which could be granted to management to deal with specific problems but there would also be a number of significant disadvantages by comparison with present arrangements. As in the case of the 'Weapons Group', the MOD could retain a degree of broad control over policy through both the constitutional arrangements for the Company and as a consequence of the Department's financial control, but this would be less than at present. Similarly, while the MOD would be able to regulate the programme to take account of changing considerations, the scope for doing this would be reduced. While an increase in management flexibility should in theory improve the prospect of programmes being completed within the planned timescales, in practice change is bound to be disruptive and this could lead to some slippage in the currently established programme in the short term. This could in turn affect the timescale for the completion of the programme in the long term, although enhanced efficiency might enable some lost time to be made up. It seems likely that in the short term there would be some additional costs to the defence budget but the scale of this cannot be judged with any certainty. Greater efficiency could produce savings in the long term, but there can be no assurance of this. The potential political and presentational difficulties of associating the civil and military nuclear programmes under one authority, the UKAEA, would not arise, but there would still be a potential presentational problem in that the completed deliverable nuclear weapon would be produced by and temporarily the responsibility of, an organisation other than the Ministry of Defence;

(c) Private Nuclear Weapons Company

The conclusions summarised at sub-para (b) relating to a publicly owned 'Nuclear Weapons Company' are also in the main valid in the case of the private Company although the potential advantages would be greater and the disadvantages more acute. Management could enjoy much greater flexibility than at present, depending on the extent to which the Company was divorced from Government control, but the weakening of MOD control over policy direction would also be correspondingly greater. The regulation of resources in the Defence Nuclear Programme to meet changing political or budgetary circumstances could be less effective; short term costs would be likely to increase but, in the longer term savings might accrue from higher efficiency. The creation of a private Nuclear Weapons Company would however involve the greatest political difficulties of all the options and these difficulties would apply not only to the Government but also affect any private industrial concern which could be found willing to assume responsibility for nuclear weapon development and production. This solution would also bring the greatest risk of disruption at the transitional stage;

(d) Civilian Manpower

The Ministry of Defence is required to make very substantial reductions in its civilian staff manpower and the transfer outside of MOD of 6000 staff, would, if acceptable (as seems possible) as a reduction in Civil Service numbers, make a significant contribution to meeting the Department's target. Moreover, it would obviate the need for further manpower increases in the Defence Nuclear Programme as work on the currently approved programme builds up. This transfer of staff could be accomplished under any of the options above. Under none of the options, however, would short term savings be expected to accrue to the Department as a result, since staff would have to be offered acceptable conditions of service in the new organisation and the costs would be reflected in the prices charged to MOD. The Department could face difficulties should it ever prove necessary to reabsorb the transferred staff. Because the Department and the new organisation would be dealing with each other as separate entities some increases in staff would be necessary in both, although within MOD there should be some marginal staff reductions in existing functions. The benefits of transferring staff would thus be presentational rather than substantial.

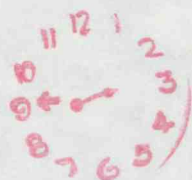
US NUCLEAR WEAPONS ORGANISATIONS

1. The US organisation for its nuclear weapon programme is different from any of those discussed in the paper. Responsibility for the US programme is divided between the Departments of Defence (DOD) and Energy (DOE). DOD specifies the nuclear weapons required for Service deployment and arranges for the production of the weapon systems (apart from the nuclear warheads and the components directly associated with them). DOD also undertakes work, and monitors the DOE programme, to ensure compatibility with the operational requirements.

2. DOE is responsible for all nuclear warhead research, development, production and assembly. Research and development on the nuclear warhead capsule is undertaken by the laboratories at Los Alamos and Livermore, which are managed by the University of California for a management fee paid by DOE; the programmes of the laboratories are, however, dictated by DOE, in conformity with policies agreed with DOD. Research and development on the electronics systems for the warhead capsule is carried out by the Sandia Corporation in dedicated facilities at Albuquerque and Livermore under a DOE 'non-profit' contract. The production of special nuclear materials, and the production of warhead components and their assembly are carried out by private companies under DOE contracts in purpose built facilities, largely owned by DOE.

3. At the moment, the US arrangements are being criticised from various directions. In particular, some critics believe that the DOE function should be taken over by DOD; others wish to divest the University of California of any relationship with the weapons programme.

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

31 October 1980

The Rt. Hon. Francis Pym MC MP
Secretary of State
Ministry of Defence

Dear Francis

You sent me a copy of your letter of 22 September to David Howell proposing a study of whether the Atomic Weapons Research Establishment might with advantage be transferred back to the Atomic Energy Authority. I have just seen David Howell's reply agreeing that an informal working group should be set up for this purpose.

I should like to take up your offer for the Treasury to be associated with the study. The financial implications of a transfer ought to be carefully considered and I should like my officials to be members of the working group.

I am copying this to the recipients of your letter.

GEOFFREY HOWE

[Handwritten signature]

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31 OCT 1980



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✓ MAP

CV

SECRETARY OF STATE FOR ENERGY
AND NUCLEAR AFFAIRS
WILLINGDALE HOUSE

01-211-6402

Rt Hon Francis Pym, MC
Secretary of State for Defence
Ministry of Defence
Whitehall
SW1

15 October 1980

See Francis

Thank you for your letter of 22 September in which you propose that an informal working group should be set up to consider the idea that Aldermaston, and possibly two nuclear Royal Ordnance Factories, should once again become part of the Atomic Energy Authority. I am of course content for officials of my Department as well as the AEA, to be represented and there are a number of important issues that they will need to examine in the light of specific proposals.

It seems inevitable, however, that any closer relationship between Aldermaston and the Atomic Energy Authority would tend to increase the association between civil nuclear power and nuclear weapons in the public mind and thus make a consensus on the need for a nuclear contribution to energy supply all the more difficult to achieve.

From my point of view, this would be a serious drawback, particularly with the prospect of a public inquiry into the Pressurised Water Reactor in 1982. Christopher Soames has said that a powerful case would be required to reverse the step that was taken in 1973. I think it would therefore be helpful if you were to circulate before the working group meets a note setting out more fully than your letter does the arguments from the defence point of view for a change.

I am copying this letter to the recipients of yours.

Howell

D A R HOWELL

Howell

Gov Mem
Sept 80

115 OCT 1980

115 OCT 1980

Civil Service Department,
Whitehall,
London, SW1A 2AZ

*With the Compliments
of the
Lord President of the Council*

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Civil Service Department
Whitehall London SW1A 2AZ
01-273 4400

8th October 1980

The Rt Hon Francis Pym, MC, MP
Secretary of State for Defence
Main Building
Whitehall
LONDON SW1A 2HB

Dear Francis,

ATOMIC WEAPONS RESEARCH ESTABLISHMENT (AWRE)

Thank you for sending me a copy of your minute of 22 September to David Howell about the future of AWRE.

As you say, the Establishment was part of the Atomic Energy Authority (AEA) until as recently as 1973. The transfer to the MOD was recommended by Sir Derek Rayner in a report which was published in the White Paper on Government Organisation for Defence Procurement and Civil Aerospace (1971 Cmnd 4641). Paragraph 86 of the Rayner report said that the transfer of the AWRE was "a pre-requisite to an economical rationalisation" of defence research and development establishments. Given the authority and reason for this recommendation, a powerful case would be required to justify returning the AWRE to the AEA.

It is this, of course, that you want the working group of officials to consider before you reach any conclusions about the AWRE's future. I am grateful to you for giving me the opportunity to be represented on the group. I do not think, however, that CSD need be full members. It would be sufficient for our purposes to receive the papers and to be able to feed in comments as necessary. My officials would be glad to brief yours on any CSD points that it would be useful for the group to keep in mind.

I am sending copies of this letter to the Prime Minister, the Chancellor of the Exchequer, the Foreign and Commonwealth Secretary and the Secretary of State for Energy, and to Sir Robert Armstrong.

Yours ever
Christopher

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SECRETARY OF STATE FOR ENERGY

I have been considering, particularly in the light of the decision to go ahead with the procurement of Trident, how we can most efficiently carry out our defence nuclear programme. Our aims and commitments on the size of the Civil Service are also relevant.

2. The Atomic Weapons Research Establishment, Aldermaston, was until fairly recently part of the Atomic Energy Authority (AEA), but was brought under the Ministry of Defence, on all fours with other MOD Research Establishments, following the Atomic Energy Authority (Weapons Group) Act of 1973. I believe that there is now a case for taking a fresh look, without preconceptions, at whether this remains the best solution; whether the advantages looked for in 1973 have been achieved; whether the balance for and against in today's (and likely future) circumstances still points the same way; and what the implications would be of reverting to the former arrangement or a modified version of it. I have an open mind on the outcome but I believe that we should now re-examine the issues, including the place in any new arrangements of the two nuclear Royal Ordnance Factories. I should like to set up an informal working group, chaired at Deputy Secretary level, to go into the implications and I should be grateful to know whether you would be willing to have representatives on this group from both your Department and the AEA.

3. I should be glad to have officials from the Treasury and the Civil Service Department associated with this study if that is what the Chancellor of the Exchequer and the Lord President of the Council, to whom I am sending copies of this minute, would wish.

4. Copies of this minute go also to the Prime Minister and the Foreign and Commonwealth Secretary; and to Sir Robert Armstrong.

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Ministry of Defence

22nd September 1980

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