PART 16.

MT.

SECRET.

Confidential Filing

The Future of the Rover Group.

in attached Folder NAO report on Sale of Rover Gp.

INDUSTRIAL POLICY

Part 1: Sept 1979.

Part 16: Jan 1989.

Referred to	Date	Referred to	Date	Referred to	Date	Referred to	Date
~~16.1.89.~~							
~~13.6.89~~							
~~6.11.89~~							
~~12.12.89~~							
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~~31-1-90~~							
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30.3.90							
PT 16 ENDS							

PREM 19/3042

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PART 16 ends:-

PG to PM 30.3.90

PART 17 begins:-

MS/DTI to SS/DTI. 2.4.90

Published Papers

The following published paper(s) enclosed on this file have been removed and destroyed. Copies may be found elsewhere in The National Archives.

National Audit Office
Report by the Comptroller and Auditor General
Department of Trade and Industry: Sale of Rover Group plc to British Aerospace plc
Ordered by the House of Commons to be printed 21 November 1989
Printed by HMSO ISBN 0 10 200990 2

Signed _____ Date 30/11/2016

PREM Records Team

CONFIDENTIAL AND PERSONAL

PRIME MINISTER

ROVER: MEETING WITH THE ATTORNEY GENERAL

The Attorney General's Office rang me today to say he would like to have a private word with you, without other Ministers present, about the position reached in the Commission's consideration of the terms of the Rover/BAe deal.

As far as I can gather, the Attorney General wants to alert you to his disquiet about the way the final stages of the Rover deal were handled. In the words of his office, 'it was all sailing too close to the wind'. You will recall that there was some flavour of this when you saw the Attorney General and Mr Ridley a few weeks back.

I am not sure what conclusions the Attorney will seek to draw. I strongly suspect he will say that there should be no question of the Government seeking to resist Commission demands for repayment of the final £33 million 'sweeteners' package. That in itself should present no particular problem; I think both you and Mr Ridley are resigned to the fact that this repayment will have to be made. What would be more difficult to handle is if the Attorney suggests that the Government should not take legal steps to resist repayment of earlier parts of the deal, should the Commission continue to press for that.

I have arranged for the Attorney to come in to see you about this next Wednesday.

Meantime, Douglas Hogg is continuing his discussion with Leon Brittan and the Commission. There was a further meeting yesterday which I understand did not go too badly. The main problem seems to be with Commission staff rather than Leon Brittan himself. It remains to be seen what final view will emerge; Leon Brittan is now reflecting and will let us know what conclusions he has reached towards the end of April. When the position is clearer you will presumably want to have a further meeting with Nick Ridley, the Chancellor and the Attorney to consider what action the Government should take.

PAUL GRAY
30 March 1990

CONFIDENTIAL AND PERSONAL

FILE : SLH

SECRET AND COMMERCIAL IN CONFIDENCE

10 DOWNING STREET
LONDON SW1A 2AA

From the Private Secretary

19 March 1990

Dear Kate,

ROVER GROUP

Thank you for your letter of 16 March enclosing notes reporting on the outcome of your Minister's meeting with Sir Leon Brittan. The Prime Minister has seen this and commented that your Minister seems to have done very well.

I am copying this letter to Stephen Wall (Foreign and Commonwealth Office), Martin Stanley (Department of Trade and Industry) and Juliet Wheldon (Law Officers' Department).

Yours,
Paul Gray

PAUL GRAY

Ms. Kate Phillips,
Minister of State,
Department of Trade and Industry

SECRET AND COMMERCIAL IN CONFIDENCE

KK

OTO.

dti

the department for Enterprise

Douglas has done very well. MT

The Hon. Douglas Hogg MP
Minister for Industry and Enterprise

Department of
Trade and Industry

1-19 Victoria Street
London SW1H 0ET

Enquiries
01-215 5000

Telex 8811074/5 DTHQ G
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COVERING SECRET
COMMERCIAL IN CONFIDENCE

Paul Gray Esq
Private Secretary to
the Prime Minister
10 Downing Street
LONDON SW1

Direct line 215 5147
Our ref
Your ref
Date 16 March 1990

Prime Minister'

You will wish to see the latest position reached with Leon Brittan, which is not without hope. Charles has alerted you separately to David Williamson's view that Douglas Hogg rather than Nick Ridley should continue to take the lead in the negotiations.

RRG 16/3

Dear Paul,

ROVER GROUP

I enclose a copy of a note the Minister has sent to the Secretary of State concerning his meeting with Sir Leon Brittan yesterday to discuss Rover Group. A full record of the meeting is also enclosed.

I am copying this, for information, to Stephen Wall (FCO) and Juliet Wheldon (Attorney General's Office).

Yours ever,

Kate Philipps

KATE PHILIPPS
PRIVATE SECRETARY

ING2080

Recycled Paper

SECRET
MARKET SENSITIVE

To:

SECRETARY OF STATE

From:

DOUGLAS HOGG

cc Sir P Gregson
Mr Williams
Mr Roberts
Mr Hosker
Mr Cochlin
Mr Thornton
Mr Stanley
Miss Carter

16 March 1990

ROVER GROUP

I saw Leon Brittan yesterday to continue our exchanges on the Rover/BAe deal. I attach the full note of the discussion prepared by Jonathan Rees (UKRep).

2 We did not dwell on the £33m special concessions. You had already told him that we would not challenge a Commission Decision that this should be repaid and he made clear yesterday that this was the minimum outcome.

3 My main purpose was to present the UK "non-paper" dealing with the Commission's complaint that Barings' advice to DTI was material information which, had it been disclosed would have led the Commission to different conclusions on the level of aid. This is the main plank for their arguing that a further £78m aid should be repaid. As you will see I argued strongly that the advice was not a valuation of the company nor, as the assumptions used by Barings were quickly overtaken by events, did we believe it material to the Commission's investigations. Most important, it was now apparent from the documents made available by Barings that the final terms agreed with BAe fell in the range suggested by Barings and indeed by Ford. The Commission were therefore most unlikely to have regarded Barings' brief as justification for reaching different conclusions on the aid.

4 In reply, Leon Brittan pointed out that the Commission were not concerned about the character of the Barings' advice, simply whether it was material and that was for the Commission to judge. He did however seem to agree that it was pertinent to ask whether, even with access to the Barings' data, the Commission would have behaved differently. This I think is the most fertile ground for argument. Interestingly he also seemed ready to concede that, on the principle of "legitimate expectation", it was arguable that BAe should not be penalised as a consequence of actions by Government of which they were unaware. Even if the Commission found their case proven, they would not necessarily insist on repayment of the £78m.

5 Overall, I formed the impression that, whilst giving nothing away, Leon Brittan remains genuinely open-minded on the arguments though he is doubtless under heavy internal pressure to put us through the wringer. There are two follow-up points:

(i) we need to decide whether to seek the opening of a formal procedure or follow the less formal route recommended by Leon Brittan. The arguments are set out in the note from Jonathan Rees. I am quite sure we should take his advice. We cannot afford the deal to be re-opened for examination by other Member States - we have few friends in all this - and the less formal route would still give us ample opportunity to press our case and leave us free to go to the ECJ. Do you agree?

(ii) there are a few non-Baring issues raised by the Commission to which we need to respond. These are in my view essentially "make-weight" items to support the Barings issue but we need to take them seriously. I have promised to provide a "non-paper" setting out our views and Leon Brittan has suggested that I meet him again in the week beginning 26 March

to run through them. This will also cover his question about whether HMG had a "floor price" in the negotiation with BAe which I am considering. Are you content with this?

DTL

CONFIDENTIAL - NAMED DISTRIBUTION ONLY PS/Mr Hogg

Reference

From: Jonathan Rees

Date: 15 March 1990

NOTE FOR THE RECORD

ROVER: MR HOGG'S MEETING WITH SIR LEON BRITTAN: 15 MARCH

SUMMARY

1. A 75 minute discussion concentrated on the issues raised in connection with Barings' advice, and HMG's views on why it does not justify amendments to the Commission's 1988 Decision. It was agreed that the UK should respond to the other points raised in the Commission's non-paper of 14 March with a further non-paper of our own to be discussed at a follow-up meeting in the week beginning 26 March. Sir Leon also outlined the Commission's views on possible future procedures, and said that even if the Commission found the aid granted illegal it might not demand repayment in total from British Aerospace.

DETAIL

2. Sir Leon Brittan was accompanied by Claus Ehlermann (Director-General, DGIV), Jim Currie (Chef de Cabinet) and Catherine Day (Cabinet Member). Mr Hogg was accompanied by Mike Cochlin (CVM, DTI), Kate Philipps (PS/Mr Hogg) and myself.

PROCEDURES

3. Sir Leon began by picking up the reference in our non-paper to a "formal reopening" of the Commission's July 1988 Decision. He said that the Commission saw two main options:

a) a formal reopening of the Decision, with full procedures for consultation with other Member States and third parties etc;

b) a less formal procedure (as the Commission had followed in the Renault case) whereby the Commission would take a decision, in the light of the new information, and Sir Leon would formally write to the Government proposing repayment of aid, giving HMG a specified time (eg two months) in which to respond.

4. In both cases, Sir Leon commented that the UK authorities would have full opportunity to comment formally on the Commission's Decision before any possible reference to the ECJ. His own strong preference was for the less formal procedure (ie b) above) - reopening the formal procedure would be much more protracted with ensuing commercial and political disadvantages; it would give opportunities for "the whole world" to comment including say Ford and Lonhro; and the procedure could not be

narrowly encompassed - in principle the whole title of British Aerospace to Rover could be raised.

5. In response, Mr Hogg formally reserved his position, noted that the UK might well wish to take any Commission decision to the ECJ, and agreed that in principle there were strong attractions in avoiding any formal procedure, and in favour of the second option. Sir Leon asked Mr Hogg to let him have a definitive view on this procedural point as soon as possible.

BARINGS' ADVICE

6. Mr Hogg then spoke to the non-paper submitted yesterday, having agreed that we would wish to submit a similar non-paper on the second range of issues raised in the Commission's non-paper yesterday. Mr Hogg also said that at this stage, as Mr Ridley had said at his meeting on 5 March, we did not wish to argue about the £33m concessions but we did feel very strongly about the £78m regional assistance. We did not believe that Barings' advice to the Government in 1988 could justify the Commission recovering this aid for the following principal reasons:

a) Barings' advice was not a formal valuation;

b) the factual assumptions on which it was based changed very shortly afterwards notably in relation to the resale of Rover;

c) no reasonable Government would have considered it necessary to disclose it to the Commission given these changes and the timetable of discussions with the Commission;

d) even if disclosed, the advice would not have altered the Commission's views;

e) out of fairness to British Aerospace, who were entitled under the principle of legitimate expectation not to expect to repay.

7. In response, Sir Leon noted that the Commission's view was not predicated on the character of Barings' advice as a formal valuation but simply whether it was material in the Commission's investigation. As for British Aerospace (point e) above) he said that the Commission "may" hold that the £78m was unlawful aid but still not expect British Aerospace to repay it. No final decision had yet been taken on this point.

a) Nature of Barings' advice

8. Mr Hogg then turned to the non-paper, and in particular Barings' letters of 7 and 14 March 1990, highlighting by quotation the facts that the NAO accepted that this advice was simply an opening negotiating position, and that it was

all very tentative, with specific references to the dependence on negotiating skills, and what might happen after acquisition. The only purpose of the information was to assist in an opening negotiation position.

9. In response Sir Leon noted that Barings had also recommended against an open sale. While he accepted Mr Hogg's comment that this was a political decision, he said that it was precisely because it was a closed sale that the UK had a special duty to give full relevant information, whether such information was oral or written: in other words an "uberrimae fidei" obligation. He continued that it was in the absence of any other formal valuations, and given that Barings' was the only advice on which the Government based its position, that the Commission attached such importance to it. The document was the only means which HMG had of assessing value for money. Mr Hogg countered that the document was in essence a steering brief to show where negotiations should be started.

10. Sir Leon then developed a line of questioning in which he tried to establish that there was a relationship between the starting figure and the valuation, and in particular that Baring's advice must have contributed to the Government's floor price (ie the price below which it would not go). Mr Hogg countered that the floor was as much to do with political presentation as value, and with the Government's wish to sell the company as a going concern. He added that it was not possible to deduce the floor price from the Barings' advice (which Sir Leon accepted). Nonetheless, Sir Leon concluded that it was difficult to take the view that Barings' advice had nothing to do with the value direct or indirect of Rover. Mr Hogg agreed to consider further whether there was anything more we could say on whether HMG had a specific floor price in mind in 1988.

b) Change in assumptions

11. Mr Hogg then outlined the significant changes in the factual assumptions on which Barings' advice had been based, in particular, the amount of debt to be written off, the restrictions on the onsale of Rover, which Barings had admitted carried significant risks, and the possible value of the tax concessions.

c) Non-disclosure

12. Mr Hogg then said that in HMG's view the Barings' advice was not a class of information which a reasonable Government would have thought to have disclosed. By the time that HMG had entered into negotiations with the Commission the assumptions on which the Barings' advice were based were no longer valid. The advice was therefore not material.

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Reference.....

13. Sir Leon said that he accepted that there was no "wilful non-disclosure". On the other hand it was for the Commission to judge whether and when a "material document" was immaterial, particularly since there was no other advice on which HMG was acting. He was therefore "not wholly persuaded" by this line of argument. But he did accept that HMG's strongest point was that even if the Commission had had this information it would not have changed its mind.

d) Content of Barings' advice

14. Mr Hogg then went through the figures in Barings' advice, demonstrating that on the basis of Barings' own advice the final cost to HMG of the sale of Rover was well within Barings' range. This was particularly so if you took into account the restrictions on the onsale of Rover. In short we believed that even if the Commission had had the Barings' advice in front of them they would not have changed their final decision. Mr Hogg continued that the figures in the Ford paper too were consistent with the final outcome. Sir Leon Brittan noted this argument.

e) Legitimate expectations

15. This point was not discussed in detail. Sir Leon simply noted that he understood that British Aerospace had a legitimate expectation that the deal would go through.

OTHER ISSUES

16. Sir Leon said that he awaited with keen interest HMG's response to the other issues raised in the Commission's non-paper of yesterday, and in particular on

a) why HMG had not given the Commission Rover's corporate plan;

b) why the Commission had not been informed of the important figures in the plan;

c) nor of the important amendments in February;

d) nor of the important amendments in June;

e) why they had only received a Bowdlerised version at the last moment in July.

Sir Leon continued that he would take a lot of persuading that this information was irrelevant, immaterial, and would not have changed the Commission's assessment. In response to Mr Hogg's question, Sir Leon said that he viewed these issues as very serious (and not just as secondary to Barings) and wanted them fully addressed.

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NEXT STEPS

17. It was agreed that we would submit a further non-paper on these latter issues by Wednesday 21 March, for discussion early the following week (Monday 26 or Tuesday 27). Sir Leon said that such discussions could be either at official or Ministerial level, though his preference would be for his direct involvement and a further discussion with Mr Hogg.

18. Sir Leon continued that he had not yet made up his mind on the whole case nor about when he would go to the Commission but he anticipated quite a quick decision following his next meeting with Mr Hogg.

Jonathan Rees

cc. PS/Mr Ridley
PS/Mr Hogg
Mr N Thornton, IEP DTI
Mr M Cochlin, CVM DTI
Mr J Stanley, DTI Sols
Mr J Kerr, FCO
Mr B Bender, Cab Office

Sir D Hannay


PM 9 0

Copy no 2

7(a-b)

dti

the department for Enterprise

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4. The Rt. Hon. Nicholas Ridley MP
Secretary of State for Trade and Industry

1. Tim Sutton Esq
Private Secretary to the
Lord President
68 Whitehall
LONDON
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NBAm

RRC6

9/3

Direct line 01 215 5622
Our ref PB5ABD
Your ref
Date 9 March 1990

Dear Tim,

ROVER GROUP

1. I should be grateful if you could ensure that this letter and enclosures are seen only by yourself and by the Lord President. No copies should be taken.

I understand that Sir Geoffrey Howe may speak to Sir Leon Brittan over the weekend.

My Secretary of State has therefore asked that the Lord President should be briefed on the present state of negotiations between himself and Sir Leon Brittan about the Rover Group state aids case, where Sir Leon is at present holding to an unexpectedly extreme view of the extent of potential repayment by BAe.

The Lord President will recall that the Commission are reviewing the sale of Rover Group to British Aerospace, in the light of the additional package of measures valued at up to £38m which the then Secretary of State, Lord Young, agreed with British Aerospace in the closing stages of negotiation on the sale. This package was not at the time notified to the Commission. The Government has argued that the measures did not constitute notifiable state aids, but accepted that the Commission might with hindsight take a different view.

In addition to requiring repayment of the major part of this package, Sir Leon Brittan has claimed that the regional element of the original notified aid package, worth £78m, should be repaid. He asserts that HMG withheld relevant information, notably a "valuation" by our advisers Barings.

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The background is set out in my Secretary of State's minute to the Prime Minister of 7 March, and my letter and attachments to Paul Gray yesterday.

Since then, in agreement with the Secretary of State the Attorney General has spoken privately to Sir Leon Brittan explaining the need for adequate legal consideration before a further meeting; this will now take place between the Minister of State, Mr Douglas Hogg (in Mr Ridley's absence in the Soviet Union) and Sir Leon Brittan, next Thursday 15 March. Juliet Wheldon's note of the Attorney's conversation is also enclosed.

Sir Leon Brittan's stance so far has been intransigent and he seems set on moving from the present informal discussions to an early decision by the Commission. Subject to further legal advice, the view here the nature and content of Barings' advice to the Department seem completely inadequate grounds for reopening the Commission's decision of 13 July 1988 approving the £78m aid. (As my Secretary of State's minute of 7 March concedes, the recovery of the major part of the additional package is quite another matter).

If they speak, the Lord President should leave Sir Leon Brittan in no doubt about the seriousness of any such decision for the Government; stress our strong belief that reopening the £78m would be misconceived; suggest that Sir Leon now has adequate material from us to demonstrate this to the Commission; and emphasise the near certainty that the Government would have to challenge the Commission's decision in public, and (again subject to legal advice) if necessary ultimately in the European Court.

It would obviously be helpful to have a read out of any conversation which may take place.

I am sending copies of this letter, without attachments, to Paul Gray, and to Stephen Wall (FCO).

2) (3)

Yours

Rosalind Cole

ROSALIND COLE
Private Secretary

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GB(A-B)

THE LEGAL SECRETARIAT TO THE LAW OFFICERS
ATTORNEY GENERAL'S CHAMBERS
ROYAL COURTS OF JUSTICE
LONDON, WC2A 2LL

LEGAL SECRETARY

1. CDP - to see
2. Cf pc. PRC6, 9/3

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Pse Martin

It seems quite clear now but this will prove very difficult.

Martin Stanley Esq
Principal Private Secretary to the
Secretary of State for Trade & Industry
1 Victoria Street
London SW1

8 March 1990

PRC6
9/3

Dear Martin,

BAE/ROVER

[Thursday]

The Attorney General spoke to Sir Leon Brittan this afternoon, as agreed with your Secretary of State.

I should be grateful if you and copy recipients would ensure that this letter is seen only by named individuals who have a strict need to know.

The Attorney emphasised that he was ringing Sir Leon Brittan on a personal and confidential basis. As Sir Leon Brittan knew, it was most unusual for a Law Officer to speak to someone outside Government on such a matter.

The Attorney said that he understood that Sir Leon Brittan had reached the view that the £78 million regional aid, given to British Aerospace as part of the Rover Group disposal, was a state aid and therefore recoverable. The Government wanted to do its best to assist the Commission on this difficult issue and the Attorney personally was anxious that no irrevocable step should be taken within the Commission until Sir Leon Brittan had had a chance to consider a reasoned argument by the DTI. He asked Sir Leon Brittan to defer putting his recommendations to the Commission until the end of next week, in order to allow a proper case to be prepared.

Sir Leon Brittan asked if the Attorney was suggesting that his meeting with Mr Ridley, planned for tomorrow, should be postponed. The Attorney said yes: in his view there was little to be gained from a further meeting until the DTI case had been worked up. It would be beter for Sir Leon Brittan to meet Mr Hogg next Thursday, 15 March.

voluminous?

Sir Leon Brittan said that the DTI had already made "luminous" representations in the course of the Commission's investigation. He wondered whether any further paper would add anything. He emphasised that the non-paper delivered to him this morning had been misconceived in suggesting that he was concerned about the failure of the UK to disclose to the Commission a document, the Ford study, of which they had been ignorant. The Attorney replied that he did not

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wish to get drawn into the detail of the case but that he hoped that Mr Hogg would indeed be able to produce some new material. Sir Leon Brittan said that it would be helpful to have any HMG paper in advance of any further meeting: the Attorney said he could not promise this.

Sir Leon Brittan concluded by saying that he would have to consult certain other people before giving the Attorney a response. His office would however get back to the Attorney's office as soon as possible. Sarah Hall subsequently rang me, saying that Sir Leon Brittan agreed to the Attorney's suggestion and that the meeting tomorrow with Mr Ridley would not therefore take place.

As you will have gathered, Sir Leon Brittan did not give the impression that it would be easy to change the view he has already reached on BAE/Rover. However, there is at least now a little time in which to work up a fully reasoned case. DTI Solicitors will, I think, by now already have sent instructions to the junior Counsel nominated by the Attorney to advise in this matter. (To correct a minor point in Rosalind Cole's letter of yesterday, these are not joint instructions with this Department). I am in touch with John Stanley about how matters should be taken forward from there.

I am copying this letter to Paul Gray (No. 10), Stephen Wall (FCO) and John Gieve (Treasury).

Yours ever,
Jane.

MISS J L WHELDON

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the department for Enterprise

The Rt. Hon. Nicholas Ridley MP
Secretary of State for Trade and Industry

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Paul Gray
Private Secretary to the Prime Minister
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Direct line 215 5622
Our ref NP1AQE
Your ref
Date 8 March 1990

Prime Minister

To see the latest developments. Not encouraging.

RMG
8/3

MT

Dear Paul

ROVER GROUP

My Secretary of State has asked me to stress the sensitivity of these matters. These papers should only be seen by named individuals with an absolute need to know.

My Secretary of State has asked me to report developments since the Prime Minister's meeting yesterday, when it was agreed that we must fight Sir Leon Brittan's proposal to seek recovery of £78 million regional aid (in addition to the major part of the additional package of measures) given to British Aerospace as part of the Rover Group disposal. It was then envisaged that there should be an early meeting between my Secretary of State and Sir Leon Brittan with lawyers present, once a firm view on the legal issues was available.

It become clear during the course of the day that, for reasons my Secretary of State understands, the Attorney General would not be able to provide a full legal view in time for my Secretary of State to make contact with Sir Leon Brittan - as he had promised to do - yesterday evening. On reflection, and in consultation with Sir David Hannay, my Secretary of State was doubtful whether the best way of dissuading Sir Leon Brittan from his present course would be a formal confrontation with lawyers on both sides. This would inevitably bring in Sir Leon Brittan's officials (his exchange with Mr Ridley has so far been confined to himself and his Cabinet) and increase the risk of damaging leaks.

Mr Ridley therefore concluded that he should himself speak to Sir Leon Brittan and ask him to reflect on informal written material to be delivered by Sir David Hannay setting out the

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factual background to our rejection of Sir Leon Brittan's proposals. This "non-paper", a copy of which is attached, should not prejudice our subsequent ability to mount a firm legal challenge, should that be necessary; but should give the Commissioner sufficient material to withdraw, should he be ready on reflection to do so.

The conversation was with Sir Leon was not encouraging. He sought to defend his use of the Ford material by claiming that Commissioner Sutherland had been unable to make use of it in negotiation because of its confidential nature, but that he would have been able to argue up the price had he been aware of Barings' own advice to the Department. Contrary to my Secretary of State's recollection of the import of their conversation on 5 March, Sir Leon said he had always recognised that the Ford material was not available to HMG. While he said he would be ready to consider the further material provided by the Secretary of State - notable amongst which is a very helpful letter from Barings explaining their own understanding of the context of their advice - he held out little prospect that he would change his mind. (Sir Leon also claimed that he had received firm legal advice supporting his stance on the £78 million).

Mr Ridley said he would be ready to discuss the matter further with Sir Leon Brittan on Friday (when he will be in London) if Sir Leon thought such a conversation would be helpful. There might however be benefit in a further period for reflection. (No meeting will be possible next week when my Secretary of State is in the Soviet Union and Poland.)

It was left that Mr Ridley and Sir Leon Brittan would speak again today. Meanwhile, our solicitors and the Law Officers' Department are jointly instructing Junior Counsel to provide the best advice available by Friday. This will immediately concentrate on Community law aspects of Sir Leon Brittan's position vis-a-vis Her Majesty's Government; advice will subsequently be needed on the Government's position in relation to British Aerospace.

Lastly, it was I understand envisaged at this yesterday's meeting that my Secretary of State might be under an obligation to alert the BAe Chairman to the present position, bearing in mind the proximity of the company's preliminary accounts for 1989, due to be published on 14 March. Our solicitors' advice, from which the Law Officers' Department do not demur is that the Government is in the present circumstances under no obligation to disclose the course of discussions to British Aerospace, and may indeed have a duty of confidentiality not to do so. Moreover, were we to choose to inform the company, they might themselves then be under a legal obligation to inform the Stock Market, thereby achieving

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precisely the publicity we wish to avoid. We have not therefore given British Aerospace any detailed account of our discussions, though we shall keep this question under review.

I am sending a copy of this letter to Steven Wall (FCO), John Greve (HM Treasury) and to Juliet Wheldon (Law Officers' Department).

Yours

Rosalind Cole

ROSALIND COLE
Private Secretary

CONSERVATION

Recycled Paper

AMENDED VERSION TO BE SUBMITTED (RE-TYPED LOCALLY) BY UKREP D

SECRET

7.3.1990

~~DRAFT~~ NON-PAPER FOR SIR LEON BRITTAN

ROVER GROUP: BRITISH AEROSPACE

1. At his meeting with the Secretary of State for Trade and Industry on 5 March, Vice-President Brittan expressed concern that, during the 1988 procedure under Article 93 (2), the UK authorities had apparently failed to disclose to the Commission material facts which, had they been known, would have influenced the Commission's Decision of 13 July 1988 on the amount of aid regarded as compatible with the common market. Sir Leon Brittan's principal concern was a study carried out by the Ford Motor Company in April 1988 on the value of Rover Group, ~~which Sir Leon Brittan assumed had been made available at the time to the Government.~~ He also mentioned a "valuation" of Rover Group which the Government had received from their financial advisers, Baring Brothers and Co Ltd.

FORD STUDY

2. The Government learned for the first time of the existence of the Ford study on 27 February this year, when the company told them it was being provided that day to the House of Commons Sub-Committee on Trade and Industry. A copy was also sent to Government. A copy of Ford's letter to the Committee Clerk is annexed. The letter notes that the study had been made available to the Commission; we understand from the company that it was provided in confidence to the Commission

on 20 June 1988.

BARING'S ADVICE

3. The Government did not seek from Barings, nor did Barings provide, a comprehensive valuation of Rover Group's assets. In preparation for its discussions with British Aerospace, the Government did however take advice from Barings on the arguments that might be deployed in negotiation with BAe. In the light of Sir Leon Brittan's comments, we have asked Barings to confirm their role in relation to this particular aspect of the sale. Their letter of 7 March (copy attached) explains the context in which their various suggestions were put forward. Their oral advice was that for the purpose of negotiation a debt-free Rover Group could be argued to be worth £950m, but that (to take into account the business risk) this should be discounted to £500m. Barings also warned that the Government should not expect in practice to realise even this sum.

4. The DTI reflected that advice in a tabular statement included in briefing for Lord Young, a copy of which has been provided to the Commission (further copy attached). In the event, however, the company was sold with substantial debt on its balance sheet.

CONCLUSION

5. In summary, the Ford assessment was available to the Commission, but not to the British Government, in June 1988.

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It was for the Commission to take such account of this as they felt relevant in coming to their decision. Barings made no comprehensive valuation of the company: their advice related to an opening negotiating position. The UK authorities did not therefore withhold evidence or documents material to the Commission's investigations. We therefore see no grounds for the Commission to recover any part of the £78 million regional aid element.

7 MARCH 1990

~~SECRET~~

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MARKET SENSITIVE

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* Barings opening counter proposal on price is based on the following valuation:

Austin Rover plant	£400m	(viewed as cost of investment in manufacturing capacity in the vehicle sector)
Tax losses	£300m	(on the assumption that Florentine would be free to sell on the businesses to trade buyers who could better utilize the tax losses.)
Land Rover	£250m	(based on price earnings ratio of 10 on forecast 1988 pre-tax profit)
	£950m	

Barings recognise Florentine are likely to want a big margin on this valuation in recognition of the risks associated with the RG businesses - especially taking into account that their own existing operations are far from risk-free





Ford Motor Company Limited

Derek D. Barron
Chairman and Chief Executive

Brentwood Essex CM13 3BW
England

February 27, 1990

Mr Andrew Kennon
Trade and Industry Committee
Committee Office
House of Commons
London SW1A OAA

Dear Mr Kennon:

In the memorandum I sent you on 14 February I referred to a preliminary study carried out by Ford staff into the value of the Rover Group at the time of its negotiations with British Aerospace.

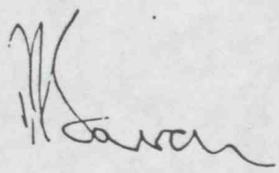
The European Commission, as part of its own inquiries into the sale of the Group, have just told us that they would like to be able to refer to Ford's position on Rover. I would like you to know that the EC Commission has the "desktop" study to which I referred in my letter to you. I think it is appropriate therefore that we should also make this available to the Trade and Industry Committee and a copy is now attached.

I must re-emphasise to you - as we have to the Commission - the reservations expressed in our memorandum about the terms of the study. It was based on limited data publicly available about the Rover Group, and the indications we developed about the range of a possible acquisition price or the capital investment required to make Rover a viable proposition were not reviewed with senior management of the Ford Group. If it had been possible to enter negotiations we would have wished to undertake a much more detailed examination.

- continued -

I would ask that in any use the Committee makes of this paper, in its report or as part of the hearings, these qualifications on the part of Ford are properly reflected.

Yours sincerely,



SALE OF ROVER GROUP TO BRITISH AEROSPACE

The British Aerospace Deal

On March 1, 1988, the British Government announced that British Aerospace (BAe) had declared a serious interest in acquiring the Government's shareholding in the Rover Group, and that the Government had granted BAe exclusive negotiating rights until April 30. On March 29, the Government announced that it had entered into a conditional contract with BAe for the sale of its 99.8 percent shareholding, subject to the approval of BAe shareholders, the Office of Fair Trading, and the European Commission.

The principal terms of the contract are as follows:

- The Government will make a £800 million cash injection into Rover Group.
- The 99.8 percent Government shareholding will be sold to BAe for £150 million.
- Tax losses of £500 million can be offset against any future Rover Group profits (out of existing tax losses of £1.6 billion).
- Government guarantees of Rover Group liabilities will be eliminated
- BAe agrees not to relinquish control of either Austin Rover or Land Rover within 5 years (no restrictions on other Rover activities or its shareholdings in Leyland-DAF, Unipart, or Istel).

Ford Interest

In late 1985, Ford initiated a study, with the support of the British Government, into the feasibility of acquiring Austin Rover. Following adverse political reaction, the Government was forced to abort discussions in February 1986. At that time, Ford had not reached a conclusion as to the desirability of acquiring Austin Rover.

Following announcement of the BAe interest on March 1, Ford of Europe decided to undertake a further internal study of Rover Group, although the Government indicated clearly that it would not consider other offers until after April 30, and only if a deal had not been concluded with BAe by that date. This study was completed on March 31.

Based on the study, Ford of Europe concluded that acquisition of Rover Group was desirable, but that it would only be feasible if the Government was willing to consider a sale to Ford. By this time, it had become clear that the Government was committed to the deal with BAe. In Ford's view, the Government would not have responded favourably to a counter bid, even at a substantially higher price than BAe had agreed. On this basis, Ford decided not to pursue its interest.

Study Approach

Ford's approach to evaluating Rover Group was to develop the cash flows that would have been generated from Ford ownership of Rover Group, and to discount these flows to derive a purchase price that would yield a sufficient return on Ford's investment. This process included the following major elements:

- A Product Plan was developed which assumed that Rover cars would maintain a unique identity, but that, over the next 13 years, Rover's existing products would be replaced by vehicles derived from Ford platforms. It was assumed, however, that the Honda-derived Rover R8 would be launched in 1989 as presently planned, and that Honda would continue to provide critical components (such as V-6 engines) for existing models until their replacement.

- A Sales Plan was developed using these product assumptions to establish Rover sales volumes over the next 10 years in all markets, and the effect of the relationship on Ford sales. In Britain (the major European market for each marque), these projections indicated some loss of market share from the combined 1987 Ford/Rover share in 1987.

- A Manufacturing Plan was then developed. To meet projected sales requirements, it was concluded that most of Rover's existing major plants would be retained, although some minor plants would be closed. Some workforce reductions would be necessary to achieve fully competitive levels of productivity. Capital expenditures required to introduce new products and for plant modernization and cost savings would be very substantial.

- Using these and other necessary assumptions, a Financial Plan was then completed, resulting in year-by-year projections of profits, capital expenditures and cash flows.

- A range of possible Purchase Prices was then calculated by discounting the cash flows using different discount factors (related to Ford's cost of capital and considerations of risk).

Study Conclusions

The study indicated that acquisition of Rover group by Ford would have been economically viable at prices substantially higher than the BAe offer, on the basis that all other terms of the BAe deal remained the same.

Because Ford of Europe would have required approval of the Company's Board of Directors to proceed further, a single proposed purchase price had not been established. In effect, this decision would have been made based on a judgement of the risks involved and the return on investment required in relation to other major investment opportunities for the Company.

However, if Ford of Europe had planned to proceed with a bid, it would have recommended an acquisition price (comparable to the £150 million BAe price) in the range £325 million to £640 million.

April 21, 1988

ROVER GROUP ANALYSIS

Purchase Price Evaluation

CASH FLOW

	1988 (Mils)	1989 (Mils)	1990 (Mils)	1992 (Mils)	1994 (Mils)	1996 (Mils)
. Profits after tax payments	£ (99)	£ (81)	£ 19	£ 52	£ 172	£ 360
. Add back depreciation	195	193	226	234	284	325
. Capitalized spending a/	(319)	(275)	(189)	(345)	(412)	(343)
. Other cash flow effects	4	38	16	11	(5)	(25)
Total Cash Flow	£(255)	£(125)	£ 72	£ (48)	£ 39	£ 317

NET PRESENT VALUE/PURCHASE PRICE

	Discount Rate 12% (Mils)	Discount Rate 16% (Mils)
. Ford Valuation of Rover Group b/	£ 400	£ 85
- Less Rover Group debt at end 1987	(560)	(560)
- Capital Injection from UK Government	800	800
Total Potential Purchase Price	£ 640	£ 325

- - - - -

a/ Capital spending less expensed amounts

b/ Net present value of projected Rover Group Cash Flow at specified discount rate

. Detailed above are the projected cash flows for the Rover Group (including Land Rover/Range Rover) following acquisition by Ford. These cash flows have been developed on the basis of the key assumptions shown opposite.

. The net present value of the cash flows has been calculated at two discount rates -- 12 percent and 16 percent. This analysis values the Rover Group to Ford at between £85 million and £400 million.

. Including the £800 million capital injection from the UK Government and the subsequent repayment of the company's existing debts (£560 million), Ford could pay between £325 million and £640 million for the Rover Group.

ROVER GROUP ANALYSIS

KEY ASSUMPTIONS

	Actual		Forecast					
SHARES/VOLUMES	1986	1987	1988	1989	1990	1992	1994	1996
Western Europe Car Industry Volume (Mils.)	11.4	12.1	11.6	11.2	11.4	11.6	11.9	12.2
UK Market Share	15.6%	14.8%	13.5%	13.5%	13.5%	12.3%	12.4%	12.2%
Western Europe Market Share	3.6%	3.5%	3.3%	3.2%	3.4%	3.3%	3.5%	3.6%
Total Car/Van Sales (incl ROW) (000)	420	472	396	395	422	406	447	455
EXPENDITURES								
. Capital Spending (Mils.)	£173	£120	£359	£309	£213	£388	£462	£386

PRICING/ECONOMICS

. Pricing -- Forward year general pricing assumptions in line with CPI projections and present Ford forward year plans

. Labor Economics -- Consistent with existing Ford plans

. Material Economics -- Consistent with present Ford projections, higher than CPI for all years

MANUFACTURING EFFICIENCIES

. Labor and Overhead -- Broadly consistent with Ford projections, adjusted to reflect differences in layout and facilities of Rover Group plants

. Material Purchases -- Higher average year purchase cost savings compared with Ford stand-alone projections reflecting the efficiencies from improved purchasing power/component commonization

OTHER

. Marketing Expense -- Progressive reduction in existing high levels of marketing expense incurred by Rover Group to average industry levels reflecting the development of fully competitive product line-up

. 'Start Up' Costs -- Profit provision of £30 million included to reflect costs of integrating the two organizations, e.g., systems

. Acquisition Terms -- As for the BAe proposal, i.e., existing debts written off through capital injection of £800 million, and tax loss carry-forwards of £500 million are available for use against future Rover Group earnings.

Baring Brothers &Co., Limited

8 Bishopsgate, London EC2N 4AE. Telephone: 01-283 8833. Telex: 883622

Strictly Private & Confidential

7th March, 1990

M. Cochlin, Esq.,
Department of Trade and Industry,
Ashdown House,
Victoria Street,
London SW1E 6RB.

Dear Mike,

ROVER GROUP

1. Following discussions between yourselves and the Commission, you asked me to set out for the Commission the basis upon which we attached a notional figure of £950 million to Rover Group at the beginning of negotiations with British Aerospace in February, 1988.

2. The key elements of this advice are accurately summarised in paragraph 3.2 of the National Audit Office Report on the transaction which was published on 21st November, 1989. That paragraph reads as follows:

> "3.2 When, in February 1988, British Aerospace confirmed their interest in buying Rover Group (paragraph 2.2), the Department of Trade and Industry sought to clarify their proposals. British Aerospace were prepared to acquire the Company in return for a net cash injection by the Government of £750 million to write-off the Group's debts. Barings advised the Department that, for negotiating purposes, a debt-free Rover Group could be argued to be worth £950 million - £400 million for Austin Rover, £250 million for Land Rover and £300 million for Rover Group's accumulated tax losses. But, to reflect the risks associated with the business, Barings suggested that the Government's opening negotiating position should be a net cash injection of £250 million - £750 million to write-off the Company's debts in exchange for a payment by British Aerospace of £500 million."

This advice was given verbally at a meeting at your offices on 23rd February, 1988.

3. Our notes - written a few days later from memory and from handwritten notes taken at the meeting - show that it began with DTI giving a briefing on the current position and on the way matters should be taken forward. I then commented on the position and made the suggestion summarised in the above extract from the National Audit Office report. I believe the Department was aware at the time that the figures we mentioned did not constitute a comprehensive professional valuation of Rover Group (nor did the Department commission such a valuation from us). In order to assist the Commission, I give below the text of our note on the advice we gave on the negotiating position.

"PB comments on possible outcome.

- Outcome very dependent on negotiating skills; HMG not in a very comfortable negotiating position.

- Florentine's freedom to deal with the business after acquisition will be important (escape route).

If £700m is to be injected at the outset, an opening negotiating position on value might be:

	£m
ARG facilities worth	400
Tax losses	300
	700
LRG @ 10x multiple	250
	950

On this basis, one might ask Florentine to pay £500m; adding £10m for minority gives total net cost to HMG of £210m. (N.B. very imprecise). Cost could rise sharply if no permission to onsell. PB stressed that this was a suggested opening negotiating position, which one would not expect to realise in practice."

In this extract, abbreviations and code names have the following meanings:

HMG - Her Majesty's Government;
Florentine - British Aerospace;
ARG - Austin Rover Group;
LRG - Land Rover Group;
PB - Peter Baring.

4. I should mention that the reference to a £700m injection (against the £750m recorded by NAO) simply reflects the uncertainties during that period about the true level of RG debt. It is also worth emphasising that our advice assumed a debt-free company.

5. Our formal advice on the disposal method was embodied in our letter to you of 29th February, 1988. In this letter we rehearsed a variety of theoretical options for the future of Rover Group - ranging from a number of disposal options to a number of other possible outcomes such as a continuation of the status quo. Our recommendation read as set out below. It must be recalled that our advice was written in our capacity as financial adviser. We were conscious that the Government had to take other issues into account - for example the effect on employment of a collapse of Rover following an abortive disposal programme - on which we were not qualified to advise. In this extract "Longbow" denotes Rover Group.

> "The surest way of evaluating the financial outcome for HMG is to ensure a degree of competition. We have recommended that Ministers make the opportunity to acquire Longbow available to at least one trade buyer in addition to Florentine for a limited period, while recognising that there is a degree of risk involved (although a lesser risk than in a prolonged auction). We recognise that HMG has decided to give weight to broader considerations in deciding not to follow this course of action."

Yours sincerely,

Peter Baring

Peter Baring

Copy no 1 of 2

6(A-D)

dti

the department for Enterprise

SECRET

The Rt. Hon. Nicholas Ridley MP
Secretary of State for Trade and Industry

Paul Gray Esq
Private Secretary to the
Prime Minister
10 Downing Street
LONDON SW1

Department of Trade and Industry

1-19 Victoria Street
London SW1H 0ET

Enquiries
01-215 5000

Telex 8811074/5 DTHQ G
Fax 01-222 2629

Direct line 01 215 5622
Our ref PB4AKL
Your ref
Date 8 March 1990

RA

ROVER GROUP: BRITISH AEROSPACE

As requested, I attach (for your files) a copy of the draft Baring's letter which my Secretary of State handed to the Attorney General on the morning of 7 March.

I also attach, again for your file, a copy of a draft non-paper which my Secretary of State might also have handed to the Attorney General.

I understand that a final version of the Barings letter has now been received here, and a late draft of the non-paper has now been sent to Sir David Hannay.

MARTIN STANLEY

Recycled Paper

ANNEX A B

SECRET

DRAFT NON-PAPER FOR SIR LEON BRITTAN

ROVER GROUP: BRITISH AEROSPACE

At his meeting with the Secretary of State for Trade and Industry on 5 March, Commissioner Brittan expressed concern that, during the 1988 procedure under Article 93 (2), the UK authorities had apparently failed to disclose to the Commission material facts which, had they been known, would have influenced the Commission's Decision of 13 July 1988 on the amount of aid regarded as compatible with the common market. The Commissioner mentioned in particular the advice which the Government received from their financial advisers, Baring Brothers and Co Ltd, and a study carried out by the Ford Motor Company in April 1988 on the value of Rover Group.

BARING'S ADVICE

2. The Government's approach to the sale of its shareholding in Rover Group has constantly been made clear, namely that it was concerned with the disposal of the company as a going concern. For this reason the Government did not seek from Barings, nor did Barings provide, a comprehensive valuation of RG's assets.

3. In preparation for its discussions with British Aerospace, the Government did however take advice from Barings on the arguments that might be deployed in negotiation with BAe. In the light of Commissioner Brittan's comments, we have asked Barings to confirm their role in relation to this particular

aspect of the sale. Their letter of 7 March (copy attached) sets out their notes of a meeting on 23 February 1988 at which their various suggestions were put forward. This includes the suggestion that a debt-free Rover Group could be argued to be worth £950m but adds that (to take into account the business risks) this should be discounted to £500m. The notes also records Barings' warning that the Government should not expect in practice to realise this sum.

The DTI's notes from this meeting took the form of a tabular statement included in briefing for Lord Young (copy attached). The Commission have already received a copy of the document.

FORD STUDY

4. In April 1988 the Ford Motor Company carried out a "desk-top" study on the potential value of Rover Group. This concluded that, on the basis of an £800m Government injection of state aid, Ford might be willing to pay a price for RG in the range of £325m - £640m. Ford have warned that the study was not reviewed by senior management, and that a final position on price could only have been established after further detailed study and "judgment of the risks involved".

5. It is interesting perhaps to note that, on the basis of Government aid of £547m, the equivalent Ford price range would be between £72m (minimum) and £387m (maximum). The £150m BAe consideration falls close to the middle of this range.

6. It is understood that Ford made a copy of the study available privately to the Commission in June 1988. The

D

Government was unaware of the study until it received a copy of Ford's letter of 27 February 1990 to the House of Commons Sub-Committee on Trade and Industry which enclosed a copy of the study.

7. We trust that the above will reassure the Commission that the UK authorities did not withhold evidence or documents material to the Commission's investigation.

ANNEX B.

DRAFT LETTER: 6TH MARCH, 1990

Strictly Private & Confidential

March, 1990

M. Cochlin, Esq.,
Department of Trade and Industry,
Ashdown House,
Victoria Street,
London SW1E 6RB.

Dear Mike,

ROVER GROUP

I am writing as requested to set out the basis upon which we attached a highly notional figure of £950 million to Rover Group at the beginning of negotiations with British Aerospace in February, 1988.

The key elements of this advice are accurately summarised in paragraph 3.2 of the National Audit Office Report on the transaction which was published on 21st February, 1989. That paragraph reads as follows:

> "3.2 When, in February 1988, British Aerospace confirmed their interest in buying Rover Group (paragraph 2.2), the Department of Trade and Industry sought to clarify their proposals. British Aerospace were prepared to acquire the Company in return for a net cash injection by the Government of £750 million to write-off the Group's debts. Barings advised the Department that, for negotiating purposes, a debt-free Rover Group could be argued to be worth £950 million - £400 million for Austin Rover, £250 million for Land Rover and £300 million for Rover Group's accumulated tax losses. But, to reflect the risks associated with the business, Barings suggested that the Government's opening negotiating position should be a net cash injection of £250 million - £750 million to write-off the Company's debts in exchange for a payment by British Aerospace of £500 million."

This advice was given verbally at a single meeting at your offices on 23rd February, 1988. It seems clear that our advice was well understood by officials, as the National Audit Office description of our comments was presumably based on a DTI note of the meeting at which they were delivered.

We similarly maintain notes of discussions as a matter of internal record. Our own note of the meeting on 23rd February - written a few days later from memory and from handwritten notes taken at the meeting - shows that it began with one of the DTI representatives giving a briefing on the then current position and on the way matters should be taken forward. Barings then commented on the position and made a suggestion as to negotiating position - the suggestion summarised in the above extract from the National Audit Office report. In order to assist you in the current situation, I can give you the text of that part of our note of the meeting which refers to our advice on negotiating position. This reads as follows:

"PB comments on possible outcome.

- Outcome very dependent on negotiating skills; HMG not in a very comfortable negotiating position.

- Florentine's freedom to deal with the business after acquisition will be important (escape route).

If £700m is to be injected at the outset, an opening negotiating position on value might be:

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ARG facilities worth	400
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On this basis, one might ask Florentine to pay £500m; adding £10m for minority gives total net cost to HMG of £210m. (N.B. very imprecise). Cost could rise sharply if no permission to onsell. PB stressed that this was a suggested opening negotiating position, which one would not expect to realise in practice."

In this extract, abbreviations and code names have the following meanings:

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Florentine - British Aerospace;
ARG - Austin Rover Group;
LRG - Land Rover Group;
PB - Peter Baring.

Our formal advice on the disposal method was embodied in our letter to you of 29th February, 1988. In this letter we rehearsed a variety of theoretical options for the future of Rover Group - ranging from a number of disposal options to a number of other possible outcomes such as a continuation of the status quo. Our recommendation read as set out below. It must be recalled that our advice was written in our capacity as financial adviser. We were conscious that the Government had to take other issues into account - for example the effect on employment of a collapse of Rover following an abortive disposal programme - on which we were not qualified to advise. In this extract "Longbow" denotes Rover Group.

> "The surest way of evaluating the financial outcome for HMG is to ensure a degree of competition. We have recommended that Ministers make the opportunity to acquire Longbow available to at least one trade buyer in addition to Florentine for a limited period, while recognising that there is a degree of risk involved (although a lesser risk than in a prolonged auction). We recognise that HMG has decided to give weight to broader considerations in deciding not to follow this course of action."

Yours sincerely,

Peter Baring

~~SECRET~~

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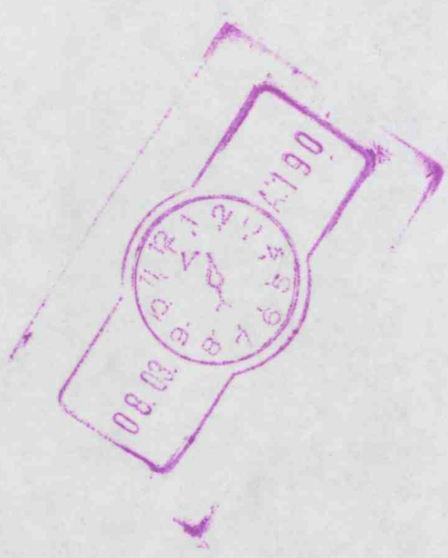
* Barings opening counter proposal on price is based on the following valuation:

Austin Rover plant	£400m	(viewed as cost of investment in manufacturin capacity in the vehicle sector)
Tax losses	£300m	(on the assumption that Florentine would be free to sell on the businesses to trade buyers who could better utilize the tax losses.)
Land Rover	£250m	(based on price earnings ratio of 10 on forecast 1988 pre-tax profit)
	£950m	

Barings recognise Florentine are likely to want a big margin on this valuation in recognition of the risks associated with the RG businesses - especially taking into account that their own existing operations are far from risk-free



SECRET AND MARKET SENSITIVE

FILE KK
5a-6
C/Economic/BAe

SUBJECT cc MASTER

10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

7 March 1990

BAE/ROVER GROUP

The Prime Minister held a short meeting this morning with your Secretary of State, the Chief Secretary and the Attorney General to discuss the position set out in your Secretary of State's minute of today's date.

I should be grateful if you and copy recipients would ensure that this letter is seen only by named individuals who have a strict need to know.

Your Secretary of State said that Barings had now made available to him a note on a relevant meeting at the beginning of the negotiations for the Government's sale of Rover to British Aerospace. This made clear that Barings' initial advice to the Government that a debt-free Rover could be said to be worth £950 million was an opening negotiating position which they "would not expect the Government to realise in practice". This note, together with Barings' willingness to confirm this view in writing to the Commission, seemed to provide further helpful material for the Government to resist the proposed repayment of £78 million of regional aid.

The Attorney General said that the Law Officers had not yet had detailed instructions on the issues raised in your Secretary of State's minute, and he could not give firm advice until this material was available. But his tentative view was that, while it would be difficult to resist repayment of £33 million of the £38 million special concessions to BAe, a case could be mounted for resisting repayment of the £78 million regional aid. The key requirement was the need to be able to demonstrate that the Commission had been in possession of all the relevant facts at the time the original decision was taken. Against that background, the Commission should be told that, armed with the relevant facts, they had accepted the terms of the exclusivity

arrangement and they could not now seek to overturn their original decision simply on the basis of hindsight.

In further discussion it was noted that your Secretary of State would be ringing Sir Leon Brittan later today with the Government's reactions to what had been said at the Brussels meeting on 5 March. But thereafter a number of options were available for putting the Government's views to the Commission: Sir David Hannay could be asked to speak to Sir Leon, your Secretary of State could make a further visit to Brussels, or an appropriate legal team could meet the Commission. It was also noted that Sir Leon Brittan was planning to take the issue to a full meeting of the Commission in about a fortnight's time.

Summing up this part of the discussion, the Prime Minister said it was agreed that the Government must resist the proposed repayment of the £78 million regional aid. The immediate objective was to seek to prevent Sir Leon Brittan and the Commission taking a firm view of the issue. Your Secretary of State would be ringing Sir Leon later today to indicate that the Government had a very strong case on this issue. Thereafter, the group were minded to think the best approach would be for your Secretary of State to go to see Sir Leon Brittan later this week with an appropriate team, probably including legal advisers. Meantime, the Law Officers should be given all the necessary material so that they could provide advice to your Secretary of State as soon as possible.

At this point the Prime Minister had to leave the meeting. Your Secretary of State said there was one further point which needed to be resolved immediately. BAe were currently in the final stages of preparing their annual accounts, but the company presently knew nothing about the possibility of the Commission seeking repayment of £78 million regional aid in addition to the £33 million special concessions. He would be grateful for the Attorney General's views on whether the Chairman of BAe should be told of this development. The Attorney General said that, given the position BAe had reached in preparing their accounts, his advice was that your Secretary of State should tell the Chairman of the company of the latest developments.

I am copying this letter to Richard Gozney (Foreign and Commonwealth Office), Carys Evans (Chief Secretary's Office) and Juliet Wheldon (Law Officers' Department).

Note Juliet Wheldon phoned me to say that, on the whole, the A-G had decided he did not wish to express a firm view on this issue one way or the other. Martin Stanley then rang me to say that DTI had concluded that they (PAUL GRAY) should not advise BAe of the latest developments.

RRG 7/3

Martin Stanley, Esq.,
Department of Trade and Industry

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the department for Enterprise

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MARKET SENSITIVE

PRIME MINISTER

BAE/ROVER GROUP

As we discussed briefly yesterday, I met Leon Brittan on 5 March to discuss the Commission's examination of the Rover Group deal.

2. He explained that he had now studied the papers and would be putting his recommendations to the full Commission in about two weeks time. He had reached the following provisional conclusions:

- £38m Special Concessions to BAe

  Apart from the £5m payment on the Columbus project (now irrelevant) he was quite clear that these were state aids and incompatible with the 1988 Decision. £33m would therefore need to be repaid and he would also need to consider adding a sum to cover interest on the £11m paid out on RG/BAe costs. I put the familiar counter-arguments but he was quite unmoved.

- Other Items

  In deciding on the approved amount of aid the Commission had accepted a £25m estimate for the increase in RG debt over the first-half of 1988. In the event, the out-turn was only £21.3m and the balance would be repayable.

Recycled Paper

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There was also the possibility of a substantial underspend on the £139m recognised in 1988 as the unspent part of the 1987 aid to cover restructuring following the Leyland-DAF commercial vehicle deal. The Commission were however ready to continue monitoring this expenditure and tackle any shortfall at a later date.

3. Leon Brittan's main concern however was the data on which the Commission had based their Decision to approve the total £547 aid package. In the 1988 negotiations the Commission were of the view that the proposed deal significantly under-estimated the value of Rover Group and only after great pressure from HMG had they agreed to increase the aid - notably by the addition of £78m "regional aid" for RG. Recent events, and the Select Committee inquiries, had proved that the Commission had been correct in their original assumptions about RG's worth. More seriously it seemed to him that HMG had withheld material facts from the Commission which, had they been known at the time, would have influenced the terms of the eventual decision. These were notably:

(i) the Barings "valuation"

The NAO report disclosed for the first time that Barings had advised the Government that a debt-free Rover would be worth £950m. HMG had not informed the Commission of this valuation;

(ii) the Ford study

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1990

The recently publicised Ford study carried out in April 1988 (which Sir Leon implied had been available to Government) also made clear that Ford would have paid substantially more for Rover Group than BAe. They were still prevented from bidding by the exclusivity granted to BAe. Other interested

Recycled Paper

parties might well have been in a similar position.

4. This failure by Government to reveal all material facts had led him to conclude that, in addition to the other items, the £78m regional aid element included in the 1988 Decision should also be repaid.

5. I have always recognised that we were vulnerable to repayment of up to £33 million of the additional package of measures, and if the Commission were to limit itself to recovery of that we might in reality have little grounds to demur. I hinted as much (privately) to Leon Brittan. But I left him in no doubt that, if he were to pursue repayment also of the £78 million we would regard it as an unfair and unacceptable decision. Barings' advice was not a formal valuation of the company - it simply provided us with arguments to deploy in negotiation with BAe - and this had been made crystal clear in the Parliamentary hearings. (Barings are helpfully prepared to confirm this in writing for the Commission.) As to the Ford study, we were only made aware of its existence a week or so ago. If, as seemed the case, the Commission knew of the study in 1988 they were free to raise it with Government but did not do so. We could hardly be faulted for not mentioning to the Commission a document of which we were unaware. There had thus been no suppression of the facts and if the Commission were to reopen the 1988 Decision it would be based simply on hindsight. This would be an unethical approach which the Government could not support.

6. We both agreed to reflect on our discussion and I promised to let him have a considered reaction by this evening. For the moment, I propose to continue arguing the merits of the case. It is possible that Leon Brittan has been manoeuvred into making these demands by internal Commission politics, in which case it makes sense for us to provide him with whatever ammunition we can to help him put the case back

Recycled Paper

dti

the department for Enterprise

on the road. I shall be instructing Sir David Hannay to return to Leon Brittan tonight with a full account of our position. I shall then myself be ready to see him again at any time. I believe it is tactically better to keep this first response low key in the hope of co-operation; but I shall not hesitate to escalate matters if that does not produce the result we need. Sir David will be armed with our best view on the legal matters raised, on which I am already in touch with the Attorney General. I am not at all sure that Leon Brittan would be on firm ground in pressing this approach.

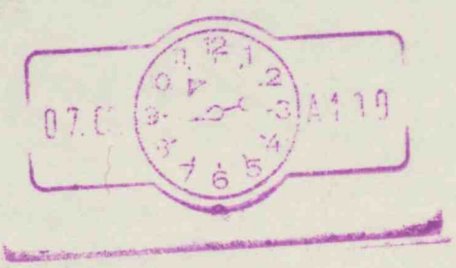
7. I am copying this minute to the Foreign and Commonwealth Secretary, the Chancellor of the Exchequer and the Attorney General.

N R

7/8 March 1990

DEPARTMENT OF TRADE AND INDUSTRY

Recycled Paper



PRIME MINISTER

ROVER

Mr. Ridley mentioned to you this morning the position reached in his discussions in Brussels yesterday with Sir Leon Brittan. He reported that the Commission were pressing for re-payment of:

(i) £33 million out of the £38 million involved in the final package of the deal;

(ii) £75 million of earlier regional aid.

On the second aspect you were both minded to fight the Commission, if necessary up to the European Court. But Mr. Ridley explained he did not need to give a response to the Commission until tomorrow night, and he wished to take further advice on the legal and other aspects before reaching a final decision.

I have now arranged for Mr. Ridley to come in again at 1110 tomorrow morning; and, following our conversation this evening, he will be joined by the Attorney General and the Chief Secretary.

PAUL GRAY

(PAUL GRAY)
6 March 1990
a:\economic\Rover (srw)

SECRET

3a-b File

SUBJECT cc MASTER

10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

6 March 1990

Dear Martin,

SALE OF ROVER

Your Secretary of State reported briefly to the Prime Minister this morning on his conversation in Brussels yesterday with Sir Leon Brittan.

I should be grateful if you would ensure this letter is seen only by those with a strict need-to-know.

Your Secretary of State said that Sir Leon had indicated the Commission would be pressing not only for repayment of £33 million out of the final package of £38 million, but also for British Aerospace to repay to the UK Government £78 million of regional grants that had been given to Rover. Sir Leon had said this was because the Commission had not at the time of the negotiations had the opportunity to see two relevant papers:

(i) the estimate prepared on Rover's potential worth by Ford;

(ii) a paper from Barings to the Department, advising on a possible evaluation for Rover that the Department might use in the opening negotiations.

Continuing, your Secretary of State said he had pointed out to Sir Leon that the first document had in fact been seen by the Commission, though it had not been given to the Department. He regarded it as quite unjustifiable for the Commission to seek to use the second document as a reason for demanding repayment of the regional grant. There appeared to be two main options open to the Government if the Commission persisted with their approach:

(a) accede to the Commission's arguments and then face a position in which BAe might refuse to make the repayment and the Government would then be obliged to take the company to court;

(b) fight the Commission's approach, if need be taking the issue to the European Court.

In brief discussion the Prime Minister and your Secretary of State indicated that they were minded to adopt the second option. But it was agreed that your Secretary of State should assemble full advice on all aspects, including an assessment of the legal prospects in the European Court; your Secretary of State would then report again to the Prime Minister on Wednesday 7 March before he went back to the Commission with his reaction.

Yours,
Paul

(PAUL GRAY)

Martin Stanley, Esq,
Department of Trade and Industry.

For information → PG

With the Compliments of

Rt. Hon. Sir Edward du Cann, KBE

GR CF

No acknowledgement p.c. R 1/2.

LONRHO Plc

RLCG 1/2

Tel: 01-606 9898

Cheapside House,
London EC2V 6BL.

LONRHO

Lonrho Plc
Cheapside House
138 Cheapside
London EC2V 6BL

Telephone 01-606 9898
Telex 885908
Telefax 01-606 2285

From: The Chairman,
The Rt. Hon. Sir Edward du Cann, KBE

January 31, 1990

Thank you for your further letter about the Rover Group.

I appreciate that you were not concerned directly with the decisions that were made by your predecessor in office. However it must be admitted that questions remain about the way in which the sale of the Rover Group was handled which to my mind have not been satisfactorily answered.

It has never been clear why British Aerospace were given the whole company without competition when other serious bidders were known to exist.

Nor is it clear why Government thought it right to sell the whole company for a net figure less than the constituent parts would have fetched. The offer Lonrho made for Land Rover and Range Rover alone was greater than the amount British Aerospace paid for the whole company.

Nor has anyone ever satisfactorily explained why Lonrho's offer for Land Rover and Range Rover was refused. An association with Lonrho would have been highly beneficial to their sales prospects.

Nor do I understand why, even if it was thought right to give British Aerospace exclusive bargaining rights over a limited period, that company's final offer was not made open to competition.

All these questions require answers.

In the absence of Lord Young I think the Department should also say why it is that Lonrho's interest in Rover was not taken seriously, as he says. We should also be told why if that was so, his private secretary wrote the letter sent to us on 15th March 1988. In the circumstances that letter was unfortunate and misleading.

Your predecessor behaved in a cavalier and irresponsible fashion over this matter.

Ministers and Departments have a duty to ensure that the public purse is protected. In the case of the sale of Rover it is absolutely plain that the best price was not attained for a very valuable asset.

Registered office as above
Registered in England No. 103002

All in all, the whole affair leaves a nasty taste in the mouth: it is undeniable that there has been incompetence. It may suit those who have been careless of the public interest to hope that the affair will be forgotten. I hope that you will issue instructions in your Department (if you have not already done so) that never again should a State-owned asset by sold for less than its realisable value and to be even-handed in its treatment of bidders, actual or potential.

Yours.

Edward.

The Rt. Hon. Nicholas Ridley, MP,
Secretary of State for Trade & Industry,
1-19 Victoria Street,
London SW1H OET

dti

the department for Enterprise

The Rt. Hon. Nicholas Ridley MP
Secretary of State for Trade and Industry

Rt Hon Sir Edward Du Cann
Chairman
Lonrho Plc
Cheapside
LONDON
EC2V 6BL

Department of
Trade and Industry

1-19 Victoria Street
London SW1H 0ET

Enquiries
01-215 5000

Telex 8811074/5 DTHQ G
Fax 01-222 2629

Direct line
Our ref 215 5623
Your ref PE4ALL
Date 26 January 1990

Dear Edward

Thank you for your letter of ~~18~~ 19 January about Rover Group.

I am not sure I can usefully add to our earlier correspondence. Your central argument remains that the Government would have received a better return if the sale of its shareholding had been the subject of competition. My letter of 7 December explained the reasons for our decision to grant limited exclusivity of negotiation to British Aerospace and this issue has also been fully explored by the Public Accounts Committee and the Trade and Industry Committee. I note your own views on the wisdom of that decision but frankly I believe no purpose would be served in speculating further on what might have transpired had the deal been open to competitive bidding.

I am copying this letter the recipients of yours.

Yours ever

Nicholas

Recycled Paper

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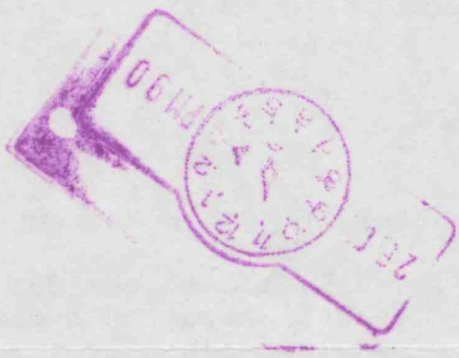

LONRHO

NBRm
RRC6
18/1

Lonrho Plc
Cheapside House
138 Cheapside
London EC2V 6BL

Telephone 01-606 9898
Telex 885908
Telefax 01-606 2285

From: The Chairman,
The Rt. Hon. Sir Edward du Cann, KBE

18th January, 1990

Dear Nicholas. at last

Thank you for your letter of 7th December commenting on my letter of November 30th, 1989 to the Comptroller & Auditor General concerning the sale of the Rover Group to British Aerospace. It appears to me that you have not been fully informed about the matter.

Your predecessor as Secretary of State, Lord Young, stated in public that the policy of the Government was to get the best price for Rover as a going concern. Also that if a higher price was available by means of asset stripping, factory closure, redundancies and the like, the Government would not pursue it. I do not imagine that any would disagree with these statements either from a business or political point of view.

However, I must say that the course adopted by Government does not appear to reflect a serious intention to obtain the best price.

If the highest price was to be raised on the above basis, it was very strange first of all to agree to grant British Aerospace exclusive bargaining rights (i.e. deliberately to exclude any other potential offer) and then even more extraordinary to proceed to sell the whole Rover Group to British Aerospace at less than a price that had been offered for part of the Group, some two years earlier. As you should know, Lonrho had made a formal offer, on 17th April 1986, of £117M for the Land Rover and Range Rover divisions. This offer was refused. No convincing commercial reason was given. The net price eventually paid by British Aerospace for the entire Rover group falls significantly below this.

The then Secretary of State refused absolutely to explore other expressions of interest in the Rover Group as a whole at the time that he made a shut-out arrangement with British Aerospace. Indeed, Lord Young stated on the radio that he did not treat seriously Lonrho's interest in the Rover Group. I do not know whether the other interested parties fared any better. Presumably they were all shut out.

/2

Registered office as above
Registered in England No. 103002

Certainly, if he did not treat seriously Lonrho's interest

(a) it was a bad commercial misjudgment, because we had been manifesting to the Secretary of State interest in the Group since 1986; and

(b) his private secretary's letter on 15th March 1988 (asking for the name of the major motor manufacturer who was jointly interested with us) was unfortunate, if not misleading.

If it is true as he says that he did not take our interest seriously, I would like to know why. Lonrho is not only one of the largest public companies in the U.K. it has a proven record of commercial success, especially in the motor trade.

Of course Lord Young could have had no basis for thinking that Lonrho's expressions of interest were on the basis of asset stripping, factory closure, redundancy or the like at Rover. Quite the reverse: Lonrho is commercially active in almost 100 countries. We are trusted with the agencies of most of the leading manufacturers of passenger and commercial vehicles, trucks and tractors. We are probably one of the largest distributors of motor vehicles in the world. Undoubtedly we could have promoted sales of vehicles manufactured by Rover to a huge extent. It is unfortunate in the national interest, and in the interests of Rover, its employees and its suppliers that the opportunity has been missed.

I say again, as was said on 15th March 1988, that the best price for the British public would have been obtained by open negotiations for Rover Plc. What happened then shows that the Secretary of State was demonstrating no commercial acuity. What has happened since shows that he also made a political misjudgment.

Incidentally, in his broadcast on the "World at One" radio programme Lord Young said that Toyota knew absolutely nothing about the offer we were making for the Rover Group. That is untrue. I can assure you that their privately expressed interest with us was real. Documents and witnesses can bear this out if need be.

To put the matter in simple terms it is clear that the Rover Group was sold to British Aerospace for a figure substantially less than the business could have realised and for less than Lonrho had already offered for Land Rover and Range Rover alone. In my view, speaking as a former Chairman of the Public Accounts Committee, the conduct of the Secretary of State at the time and of his Department is open to serious criticism.

I am sending copies of my letter to the Comptroller & Auditor General, the Chairman of the Public Accounts Committee, (the Right Honourable Robert Sheldon, MP,) the Private Secretary to the Prime Minister, and the Private Secretary to the Leader of the Opposition and the Chairman of the Select Committee on Trade & Industry.

Yours,
Edward.

Rt. Hon. Nicholas Ridley, MP,
Secretary of State for Trade & Industry,
1 Victoria Street,
London SW1H OET

Land Pol: Rover ...
Pt 16



LONRHO

Lonrho Plc
Cheapside House
138 Cheapside
London EC2V 6BL

Telephone 01-606 9898
Telex 885908
Telefax 01-606 2285

Directors:
The Rt. Hon. Sir Edward du Cann, K.B.E. *Chairman*
R. W. Rowland *Managing Director and Chief Executive*
R. G. Badger, F.C.A.
R. F. Dunlop
N. Kruger (*Zimbabwean*)
M. J. J. R. Leclezio (*Mauritian*)
T. J. Robinson, F.C.A.
P. G. B. Spicer
P. M. Tarsh, F.C.A.
R. E. Whitten, F.C.A.
Sir Peter W. Youens, C.M.G., O.B.E.

No need for any No. 10 response.
RRCG 24/1
R23/1

From: The Chairman
The Rt. Hon. Sir Edward du Cann, KBE

18th January, 1990

Dear Nicholas.

Thank you for your letter of 7th December commenting on my letter of 30th November, 1989 to the Comptroller & Auditor General concerning the sale of the Rover Group to British Aerospace. It appears to me that you have not been fully informed about the matter.

Your predecessor as Secretary of State, Lord Young, stated in public that the policy of the Government was to get the best price for Rover as a going concern. Also that if a higher price was available by means of asset stripping, factory closure, redundancies and the like, the Government would not pursue it. I do not imagine that any would disagree with these statements either from a business or political point of view.

However, I must say that the course adopted by Government does not appear to reflect a serious intention to obtain the best price.

If the highest price was to be raised on the above basis, it was very strange first of all to agree to grant British Aerospace exclusive bargaining rights (i.e. deliberately to exclude any other potential offer) and then even more extraordinary to proceed to sell the whole Rover Group to British Aerospace at less than a price that had been offered for part of the Group, some two years earlier. As you should know, Lonrho had made a formal offer, on 17th April, 1986, of £117m for the Land Rover and Range Rover divisions. This offer was refused.

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Certainly, if he did not treat seriously Lonrho's interest

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I am sending copies of my letter to the Comptroller & Auditor General, the Chairman of the Public Accounts Committee (the Right Honourable Robert Sheldon, MP), the Private Secretary to the Prime Minister, and the Private Secretary to the Leader of the Opposition and the Chairman of the Select Committee on Trade & Industry.

Yours.

Edward.

Rt. Hon. Nicholas Ridley, MP,
Secretary of State for Trade & Industry,
1 Victoria Street,
London SW1H 0ET

CF- BA RLCG 21/12

PERSONAL

cc- M. Gray (No 10)
PS/ CoF Exc
PS/SS/DTI.

PM

Prime Minister

RLCG 20/12

c- M. Whetnall

CABINET OFFICE

70 Whitehall London SW1A 2AS
01-270 0101

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

Sir Robin Butler KCB CVO

Ref. A089/3292

18 December 1989

Dear David,

Following our meeting with the Prime Minister and Nicholas Ridley on 12 December, I have been in touch with Peter Gregson and Neil Thornton about your request for advice on the invitations you have received from both the PAC and the Trade and Industry Select Committee to give evidence on the sale of Rover Group.

I attach draft replies to these invitations which you might like to consider. As we discussed, there is nothing you would want to add to evidence already given to the PAC, and it would set a precedent if you as a former Minister were to appear before them. The same considerations do not arise in relation to the Trade and Industry Select Committee to whom you have given evidence before and who are concerned with the policy aspects of the sale. The DTI will, of course, provide you with whatever assistance you require in preparing to give evidence. I spoke to Brian Hayes on the telephone on Friday, who told me that he will be accepting the Select Committee's invitation to appear on 17 January, making clear that he now does so as a private individual and not on behalf of the Government. I understand from him that his evidence will be entirely supportive.

With best wishes,

Yours ever,

Robin

The Rt Hon Lord Young of Graffham
House of Lords

PERSONAL

c- Miss Bell

Fax No 222-0023.

Draft of 18 December 1989

DRAFT REPLY FROM LORD YOUNG OF GRAFFHAM TO THE RT HON ROBERT SHELDON MP, CHAIRMAN, PUBLIC ACCOUNTS COMMITTEE, HOUSE OF COMMONS

Thank you for your letter of 13 December, giving me the chance to comment on your enquiry into the Sale of Rover Group. Following my appearance before them in May 1988, you will probably be aware that the Trade and Industry Select Committee have decided formally to invite me to give further oral evidence.

I have studied Sir Peter Gregson's evidence before your Committee on 4 December, together with Nicholas Ridley's statement to the House on 30 December and the Comptroller and Auditor General's Report and Memorandum on the sale prepared on the basis of the National Audit Office's examination of the papers of the Department of Trade and Industry.

Given the full evidence which the Public Accounts Committee has received on the circumstances surrounding the sale, the Trade and Industry Committee's formal invitation - which I shall be accepting - and the constitutional novelty which my presenting evidence,

orally or in writing, to the Public Accounts Committee would represent, I believe that there is nothing that I need to add to the deliberations of your Committee.

I am however grateful to you for offering me the opportunity to do so.

DRAFT LETTER FROM LORD YOUNG TO ANDREW CANNON ESQ

Clerk
Select Committee on Trade and Industry
House of Commons
LONDON SW1A 0AA

Thank you for your letter of 13 December.

I confirm that I shall be available to give evidence before your Committee on the morning of Wednesday 17 January, and look forward to doing so.

In view of your Committee's invitation, and other considerations, I have decided against putting separate evidence to the Public Accounts Committee, who helpfully offered me an opportunity to do so.

PE4AHX

dti

the department for Enterprise

The Rt. Hon. Nicholas Ridley MP
Secretary of State for Trade and Industry

Miss Sonia Phippard
Private Secretary to Sir Robin Butler
Cabinet Office
70 Whitehall
LONDON
SW1A 2AS

Department of Trade and Industry
1-19 Victoria Street
London SW1H 0ET
Enquiries 01-215 5000
Telex 8811074/5 DTHQ G
Fax 01-222 2629

Direct line 01 215 5622
Our ref PB4AGY
Your ref
Date 14 December 1989

Dear Sonia

LORD YOUNG'S INVITATIONS FROM SCTI AND PAC

I enclose copies of the invitations Lord Young has received from the Chairman of the PAC and from the Clerk to the Trade and Industry Committee, both of 13 December.

Following the meeting at Number Ten between the Prime Minister, Lord Young, my Secretary of State and Sir Robin Butler on 12 December, Lord Young has asked me to seek guidance for him from the Cabinet Secretary on his response to these letters.

Having taken advice from Sir Peter Gregson, I had an opportunity to discuss Lord Young's preferred response with him yesterday (at a long-arranged lunch as his ex-Private Secretary). I attach an outline of the sort of replies Lord Young and I discussed yesterday, without commitment. Their aim is sufficiently to meet his personal wish to be open with Parliament and the public, while at the same time avoiding unhelpful precedents in relation to the Public Accounts Committee. The drafts have not of course been seen by Lord Young.

Unless he hears otherwise, Lord Young will expect next to see Sir Robin's advice on an appropriate response to both letters.

Lord Young will in the course of normal business be seeing the Prime Minister on Monday, and may raise this. I am therefore sending a copy of this letter and attachments to Paul Gray, as well as to Sir Peter Gregson.

Yours ever,
Neil Thornton.

NEIL THORNTON
Principal Private Secretary

Recycled Paper

DRAFT REPLY FROM LORD YOUNG TO THE RT HON ROBERT SHELDON MP

Chairman, Public Accounts Committee
House of Commons
LONDON SW1A 0AA

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I have studied Sir Peter Gregson's evidence before your Committee on 4 December, together with Nicholas Ridley's statement to the House on 30 December and the Comptroller and Auditor General's Report and Memorandum on the sale.

Given these full accounts of the circumstances surrounding the sale, the Select Committee's formal invitation - which I shall be accepting - and the constitutional innovation which my presenting evidence, orally or in writing, to your Committee would represent, I believe that there is nothing that I need to add to the deliberations of your Committee.

I am however grateful to you for offering me the opportunity to do so.

PE4AHX

DRAFT LETTER FROM LORD YOUNG TO ANDREW CANNON ESQ

Clerk
Select Committee on Trade and Industry
House of Commons
LONDON SW1A 0AA

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I confirm that I shall be available to give evidence before your Committee on the morning of Wednesday 17 January, and look forward to doing so.

In view of your Committee's invitation, and other considerations, I have decided against putting separate evidence to the Public Accounts Committee, who helpfully offered me an opportunity to do so.

PE4AHX

Rt Hon Robert Sheldon MP

COMMITTEE OFFICE
HOUSE OF COMMONS
LONDON SW1A 0AA
01-219 3618 (Direct Line)
01-219 3000 (Switchboard)

COMMITTEE OF PUBLIC ACCOUNTS

13 December 1989

Dear Lord Young

Sale of Rover Group

You are doubtless aware that the Committee of Public Accounts took oral evidence from Sir Peter Gregson on 4th December on the subject of the Report by the Comptroller and Auditor General on the sale of Rover Group.

The Committee considers that you should be invited to comment on this subject, and I am therefore writing to ask whether you wish to submit a memorandum to the Committee on the sale. If you do decide to send a memorandum to us, the Committee may then invite you to give further, oral evidence.

The Committee has a very full programme of meetings in the New Year, so perhaps I should mention that if we were to invite you to give oral evidence, we would suggest Wednesday 10 January as a suitable date.

I look forward to hearing from you in due course.

Yours sincerely

Robert Sheldon

Robert Sheldon
Chairman

The Rt Hon Lord Young of Graffham
House of Lords

COMMITTEE OFFICE
HOUSE OF COMMONS
LONDON SW1A 0AA
01-219 5469 (Direct Line)
01-219 3000 (Switchboard)

TRADE AND INDUSTRY COMMITTEE

13 December 1989

The Rt. Hon. Lord Young of Graffham
Conservative Central Office
32 Smith Square
London SW1P 3HH

Dear Lord Young,

As you know, the Trade and Industry Select Committee took oral evidence on the sale of Rover Group to British Aerospace on four occasions in May and November 1988. In the ensuing year we have watched with interest the fortunes of the Rover Group. Now evidence has been given to the Public Accounts Committee about various aspects of the original sale which were not drawn to our attention at the time.

The Committee has therefore decided to invite you to give further oral evidence, both on the wider consequences of the sale and on details which were not known to us at the time.

The Committee is planning to hold one oral evidence session on this subject on the morning of Wednesday 17 January 1990 starting at 10.45 a.m. The others being invited to give evidence are Sir Brian Hayes, Professor Roland Smith and Sir Graham Day. It has not yet been decided whether witnesses should appear as a group or individually.

The timing of this session is intended to avoid direct overlap with evidence being sought from you by the Public Accounts Committee.

The Chairman has asked me to apologise if you first heard of this information through the press. I am writing to you directly after the meeting but (since the Committee was taking evidence in public directly after the deliberative meeting at which the decision was taken) a brief statement was made saying that you would be invited to give evidence on this subject early in the New Year.

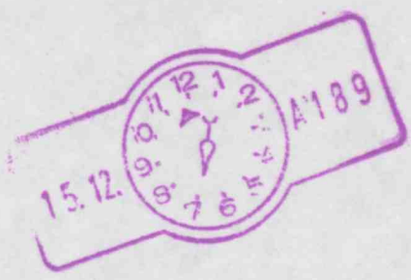
I should be grateful if you would confirm as soon as possible that you will be available to give evidence on the morning of Wednesday 17 January.



Yours sincerely,

Andrew Kennon

ANDREW KENNON
Clerk of the Committee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mem

10 DOWNING STREET
LONDON SW1A 2AA

From the Private Secretary

14 December 1989

ROVER GROUP:
SELECT COMMITTEE ON TRADE AND INDUSTRY

Thank you for your letter of 13 December, which the Prime Minister has seen and noted.

I am copying this letter to John Gieve (HM Treasury) and to Sonia Phippard (Cabinet Office).

PAUL GRAY

Neil Thornton, Esq.,
Department of Trade and Industry

6

dti

the department for Enterprise

CCPM

The Rt. Hon. Nicholas Ridley MP
Secretary of State for Trade and Industry

Paul Gray Esq
Private Secretary to the
Prime Minister
10 Downing Street
LONDON
SW1

Prime Minister

As foreshadowed when you discussed the position on the PAC with Lord Young yesterday.

Department of Trade and Industry
1-19 Victoria Street
London SW1H 0ET
Enquiries
01-215 5000
Telex 8811074/5 DTHQ G
Fax 01-222 2629

Direct line 01 215 5622
Our ref PB3AHM
Your ref
Date 13 December 1989

PRCC 13/12

Dear Paul,

ROVER GROUP - SELECT COMMITTEE ON TRADE AND INDUSTRY

During today's examination of my Secretary of State on special shares, the Chairman of the Select Committee on Trade and Industry, Mr Kenneth Warren, said his Committee would be calling back four witnesses because of recent developments on Rover Group:

Lord Young
Sir Brian Hayes (DTI's then Permanent Secretary)
Professor Roland Smith - BAe Chairman
Mr Graham Day - Rover Chairman

There was no indication that the Committee intended to call Mr Ridley or DTI officials.

I understand from Lord Young's office that he has been invited to appear on 24 January. The Department will of course give all possible support to Lord Young, consistent with the normal proprieties, in preparing for the hearing.

I am sending a copy of this letter to John Gieve (HM Treasury) and to Trevor Woolley (Cabinet Office).

Yours ever,

Neil

NEIL THORNTON
Private Secretary

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CONFIDENTIAL

file
to c: Young

10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

SIR ROBIN BUTLER

PAC HEARINGS ON ROVER

I was rung this evening by Lord Young who reported he understood the PAC had this afternoon decided to invite him to give evidence to them on 10 January. Lord Young said that, if this was confirmed, he would want to have formal guidance on how he should handle the request. He told me that, when he was in Tokyo, he had given an informal indication that, if asked, he would want to appear before a Select Committee; but what he had in mind was to appear before the Trade and Industry Select Committee rather than the PAC. His understanding was that rather different rules applied to the PAC, with the convention that that committee usually took evidence from Accounting Officers rather than Ministers (or former Ministers).

2. I took delivery of Lord Young's request. The purpose of this minute is to pass on to you the formal request from Lord Young for guidance.

3. Lord Young will in fact be seeing the Prime Minister on other matters at noon tomorrow (Tuesday). I imagine it will not be possible to provide guidance in advance of that meeting.

4. I am copying this minute to Neil Thornton (Department of Trade and Industry).

PG

11 December 1989

CONFIDENTIAL

PRIME MINISTER

Gordon Brown's letter to you attempts to blow life into the embers of Labour's attack on the Rover BAe deal. Nick Ridley's advice - which I think is right - is that he should respond to he substance of Gordon Brown's letter on the element of Rover's tax losses leaving you to send a short covering letter,* simply making clear that you did indeed know the main terms and conditions of the BAe Rover deal. The letter which, subject to your approval and comments and those of the Financial Secretary to the Treasury, Nick Ridley proposes to send tomorrow morning is at Flag A.

* attached immediately below

You will want to look through this although it seems to me a solid defence which should take the wind out of Mr. Brown's sails.

DOMINIC MORRIS
11 DECEMBER 1989

c:\wpdocs\parli\rover.mrm

dti

the department for Enterprise

The Rt. Hon. Nicholas Ridley MP
Secretary of State for Trade and Industry

Gordon Brown Esq MP
House of Commons
LONDON
SW1A OAA

Department of Trade and Industry

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Direct line 215 5422
Our ref PE1ACP
Your ref
Date December 1989

Thank you for your undated letter received over the weekend. I have also seen your related letter to the Prime Minister.

The sale of the Government's shareholding in Rover Group is the subject of a detailed enquiry by the Public Accounts Committee, and the Comptroller and Auditor General and his staff have had complete access to all of my Department's documentation relevant to the financial and other conditions of the sale. As a consequence the C & AG's reports to the PAC have addressed all the material issues. If however the PAC wishes to ask the National Audit Office to re-examine any of the papers, my Department would again be happy to offer them the fullest cooperation and access. I am also happy to consider providing the Committee direct with copies of any relevant documents they feel are necessary to pursue their inquiry. I have already received a request to provide certain documentation concerning my predecessor's exchanges with BAe last July and I am today making these available both to the Public Accounts Committee and the Select Committee on Trade and Industry. You also asked for this correspondence and I am prepared in this case to agree your request.

It seems from your public statements and the Parliamentary Questions you have tabled over the last few days that you are particularly interested in the tax aspects of the deal. I shall of course be replying to your detailed questions in the normal way but perhaps I can take this opportunity to clarify the general position.

As you will be aware there are three separate elements involved. The first are the tax losses which the Rover Group was entitled to carry forward against the profits of the same trade in the same way as any other UK company. These were

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estimated at the time of the deal to amount to £1.6bn. Our conditional agreement with BAe announced on 29 March 1988 limited the use of these to £500m, thus effectively denying Rover Group the benefit of about £1.1bn. These allowances can only by statute be utilised in the same trade ie the trade carried on in Rover Group before its acquisition. These provisions remained unchanged in the final agreement.

The other two elements are disclaimed capital allowances and capital losses. Under normal tax law, these would have been available to the enlarged Group under the same conditions and to the same extent as for any other UK group. The March conditional agreement effectively "ring-fenced" them so that they could only be utilised within the Rover Group businesses. However following the cutback in the cash injection insisted upon by the Commission, this contractual ring-fencing was lifted, thereby restoring the position to that which properly applies under statute to any other company. As was explained in the Parliamentary Statement on 14 July 1988, estimating the value of restoring that freedom was a matter for British Aerospace.

There could be no objective assessment at the time because the value would depend on the extent and timing of taxable events ensuing in the future. Different experts would ascribe different values if asked to make an estimate. The Commission, in the first week of July, internally ascribed a notional figure of £25m on the basis of available information but it was recognised by all parties that this was only one of a range of possible values; indeed the Commission were alerted to the possibility that higher estimates might subsequently emerge. In the final negotiations with British Aerospace on 12 July 1988, the company said that the change would probably be worth closer to £35m but this was again no more than a subjective estimate. Touche Ross commented on these matters in Appendix 2 to the main NAO report and you will see that they assigned a value of £33-40m for all of RG's tax benefits <u>including the trading tax losses</u> (which the other two estimates above did not). These three widely differing estimates underline the difficulty of giving precise figures in this area.

I must stress that these estimates simply represent attempts to reach a judgement on the potential benefits to BAe of exercising their normal rights under tax law. Thus there is no question of "an extra £10m in tax concessions". They are not negotiated figures. Only time will establish the true figure. Moreover they are all made clear in the NAO Report and Memorandum, so you are not raising any new matter.

The Inland revenue agreed that they would stand ready to clarify the normal tax implications of British Aerospace's

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acquisition of Rover Group, and to give later guidance of the applicability, under normal principles, of Section 768 of the Income and Corporation Taxes Act 1988 to possible future rearrangements of the Rover trades following acquisition. As you will see from the enclosed correspondence between British Aerospace and the Inland Revenue the governing principle, which British Aerospace explicitly shared, was that the tax treatment of anything concerning the Rover acquisition must be consistent with the law and the treatment of other taxpayers in comparable circumstances. British Aerospace have not had and have not been promised any concessions over their tax liabilities - these will be determined in accordance with normal principles.

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Gordon Brown M.P.
Member of Parliament for Dunfermline East

PS

already dealt with

HOUSE OF COMMONS
LONDON SW1A 0AA

CB/12

Rt Hon Margaret Thatcher MP
Prime Minister
lO Downing Street
London

Dear Prime Minister

Following your answer in the House today, it is now imperative that the full facts about the Government's sale of Rover be disclosed.

I am therefore asking you to make available the relevant final agreement on cash, assets and tax signed between the Government and Aerospace and to make available the correspondence between Lord Young and British Aerospace during July 1988.

I hope you will now tell us whether you were aware of the terms of the final deal , including the hidden subsidies, and of the deception of Parliament and the European Commission including the assessment that was made within your Government of the risks of being found out

Yours faithfully

Gordon Brown

Gordon Brown
Labour Trade and Industry spokesman

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the department for Enterprise

The Rt. Hon. Nicholas Ridley MP
Secretary of State for Trade and Industry

. Rt Hon Sir Edward du Cann
Lonrho plc
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Our ref JW1AFM
Your ref
Date 7 December 1989

Dear Edward

Thank you for copying to me your letter of 30 November to John Bourn.

As far as I am aware the Department's position on other expressions of interest in Rover Group has been clear and consistent throughout. As was explained in the Parliamentary statement of 29 March 1988 and in more detail in evidence to the Select Committee on Trade and Industry in May of last year, there were four expressions of interest received during the exclusivity period, of which Lonrho's was of course one (there were however no specific offers). When their expressions of interest were received, all four companies were simply reminded of the Parliamentary Statement of 1 March 1988 in which the Government announced it had agreed a period of two months in which it would negotiate exclusively with British Aerospace. If those negotiations had not led to an agreement, then the Government would have been ready to hold discussions on alternative proposals: but while the exclusivity policy remained in force, it would have been a breach of our word if we had departed from it.

It was quite clear from the second letter which Lonrho wrote to my predecessor that the company wanted him to reconsider the exclusivity agreement; they were of course fully entitled to urge that but the Government stood by its original decision, taken with the full agreement of the Rover Group Chairman, because opening up the sale process to auction would have been damaging to the Rover businesses. Neither Lonrho nor any of the other three expressions of interest came back with a specific offer. You say in your letter that this was because the companies were denied access to information. The Government considered that, because of the commitment to

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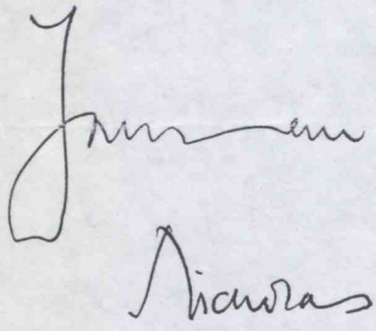
negotiate only with British Aerospace, it was not appropriate at that stage to make available information on Rover Group to other parties.

I am copying this letter to the recipients of yours.



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P/A

To: Mr Thornton

From : Peter Bunn

CVM5
215-6489
2 Dec 89

cc Sir Peter Gregson
Mr Cochlin
Miss Neville Rolfe
Miss Maclean
Miss Carter
Mr Revolta

PAC Briefing

As background to the 1200 meeting on Monday you asked for sight of the key briefing material for Sir Peter as amended for Thursdays events. This is now attached although in the time available we have not attempted to reshade every answer on paper. What we have sought to do is to work on the basis that the PAC will publish the whole of the transcript of what will start formally as private and public sessions; we have therefore ironed out a lot of references which could exacerbate Brussels relations.

The Q and As were structured to tie in with the order of the NAO Report and the memorandum. To aid travel through the resulting maze we have prepared a quick index as the top sheet. In general all the key issues of the NAO report are covered in the section dealing with the NAO summary: questions 1-24. The supplementary memorandum questions from 72 to the end are also note-worthy.

For copy recipients used to the previous edition major changes and additions are sidelined.

For convenience I am circulating under this note the tables of RG profitability and market share, and note on Shorts and water clawback terms (which were outstanding remits) - the latter emphatically not for comment during the current offer period.

P L Bunn

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QUICK GUIDE TO KEY QUESTIONS	Nos>72 for resticted session
Additional terms	72-75 General,81-89 individually
Associated Stakes	18,52(Daf/Istel),104(barings table)
Barings	
excl and lim auc	2,13,
950m	30,
Change in terms Mar-Jul	53-6
Clawback	20,
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VMJ	11-12

888-273

NAO REPORT : QUESTION AND ANSWER BRIEF

SUMMARY AND CONCLUSIONS

Background.

para 1 . 'entered into exclusive negotiations

(see also brief 1)

Q1. WHY WERE BAE GRANTED EXCLUSIVE NEGOTIATING RIGHTS ?

A1. It was a policy decision by Ministers to accept BAe's condition of exclusivity. Competitive bidding would almost certainly have given rise to the sort of political controversy that had previously been so damaging to the commercial prospects of Rover Group. This would have undermined the realisable value of the business and put broader policy objectives at risk.

Q2. WHY DID YOU REJECT BARINGS' ADVICE THAT AT LEAST ONE OTHER BIDDER SHOULD BE ALLOWED TO BID AND ESTABLISH A MARKET PRICE ?

(see also Q13)

A2. Seeking to negotiate in secret with one other bidder might in theory have reduced (but not eliminated) the risks; however it would not have been possible to draw up defensible criteria that excluded all but one bidder. The only realistic alternative to exclusivity was a general auction which, Barings agreed, would have been very commercially damaging to Rover Group.

para 1. 'exclusive negotiations with British Aerospace'

(see also brief 1)

Q3. WHY WAS BRITISH AEROSPACE SELECTED ?

A3. BAe was the only company to make a bid.] SEE NEW Q78B]

Q4. WHAT ABOUT THE OTHER COMPANIES WHICH EXPRESSED AN INTEREST

(see also Qs 14 & 15. For line to take on individual bidders see Qs 76 to 80)

A4. None of them made an offer

Q5. HOW COULD ANYONE BUT BAE MAKE AN OFFER WITHOUT ACCESS TO INFORMATION ?

A5. RG was a listed company with a high profile in a much analysed sector and a considerable amount of information was readily available. We do not believe that information was an unsurmountable obstacle to an offer, especially from companies in the industry who tend to keep their own intelligence on competitors' performance.

Q6. WOULDN'T A MOTOR MANUFACTURER HAVE BEEN PREPARED TO PAY A HIGHER PRICE THAN BAE ?

A6. That is a hypothetical question because Ministers decided to negotiate exclusively with BAe. It is certainly possible that a business already established in the UK motor industry would have valued RG more highly, though the likelihood that they would need to rationalise the business more to fit their existing operations means that this is not a foregone conclusion. A sale to such a business would have raised competition issues as well as political controversy, exposing RG to a period of prolonged uncertainty. The options for a sale to a motor manufacturer were in any case complicated by the assurance given by the then Secretary of State, Mr Channon, in the House in February 1986, that,in order to end the damaging uncertainty, the possibility of a sale of Austin Rover to

Ford, the most likely suitor, would not be pursued. At no point had Ministers indicated a willingness to backtrack on that.

Note: PQs in 1987 about Ford received replies to the effect that the position was unchanged from the 1986 statement. More general privatisation PQs were dealt with by reference to the review of options by Sir Graham Day. In response to a specific question about a foreign takeover CDL (Mr Clarke) replied on 24 November 1987 that in considering any proposal he would consider the long term prospects of RG to be more important than the nationality of the owners.

Q7. WHY WERE MINISTERS NOT PREPARED TO OFFER AUSTIN ROVER TO FORD BUT WERE PREPARED TO SEE FORD TAKE OVER JAGUAR ?

A7. There was strong Parliamentary opposition to a privatisation by means of the sale of Austin Rover and Land Rover to foreign competitors and the public and political controversy was threatening to harm the companies. Jaguar was privatised in 1984 and had had five years of protection from predators when it bacame the target of a full bid from Ford and a partial bid from General Motors. In these circumstances the Secretary of State decided that he would end the damaging speculation about the use of the golden share and clear the way for the future of the company to be decided by the shareholders, not by Ministers whose interest would be confined to considering any competition policy aspects of any deal which might be struck.

Q8. WHAT WOULD YOU HAVE DONE IF ANOTHER BIDDER HAD OFFERED A HIGHER PRICE DURING THE EXCLUSIVITY PERIOD ?

A8. Exclusivity was a declaration of intent and did not bind HMG

to accept the outcome of negotiations. The receipt of a better offer would have been an important factor in deciding whether or not to accept BAe's offer.

Q9. DIDN'T THE PUBLIC ANNOUNCEMENT OF EXCLUSIVE NEGOTIATIONS WITH BAE PUT HMG INTO A WEAK NEGOTIATING POSITION ? IF NEGOTIATIONS HAD BEEN IN SECRET AT LEAST HMG COULD HAVE WALKED AWAY WITH NO LOSS OF FACE IF ACCEPTABLE TERMS COULD NOT BE AGREED.

A9. Experience of the commmercial vehicle privatisation had shown the advantage of pre-emptive statements of intent about RG privatisations; the risks of a leak would have been unacceptable once detailed negotiation, due diligence work etc. was put in hand. It could also be argued that the loss of face argument would apply equally to the Board of BAe. A further factor BAe would have been aware of was RG's management work on a placement option, so they knew they were not the only route to RG's privatisation.

On the granting of exclusive negotiating rights to British Aerospace

para 4 (a) : 'the benefits of competition were outweighed by the <u>risk to Rover Group's prospects</u> arising from uncertainty that would be associated with a competitive sale'

Q10. HOW REAL WAS THE RISK TO ROVER GROUP OF COMPETITIVE BIDDING?

A10. Experience has shown that RG is very vulnerable to political controversy and uncertainty about its future. During the deliberations over the 1985 Corporate Plan Austin Rover's share of the UK car market fell from 19.3 % in April to 15.8% in June. There

was then a partial recovery until disclosure early in 1986 of Ford's bid for the company when market share fell from 18.4% in January to 15.8% in February. Austin Rover has never recovered that lost share of the market and Sir Graham Day and his Board advised us that any further controversy would cause severe, possibly irreparable, damage to the business

If pressed

Q10a BUT SINCE THEN RG'S MARKET SHARE HAS FALLEN FURTHER WITHOUT SUCH DAMAGE?

A10a The point is that,because of the strong growth in the market, volume and profitability have held up. Market share is a commonly used statistic but it needs careful interpretation in the context of the market as a whole.

para 4 (a), : 'A failure of Rover Group could crystallise the Government's obligations to the Company's creditors'

Q11. WHAT WAS THE EXTENT OF THOSE OBLIGATIONS?

(see background note 12)

A11. The maximum amount of outstanding domestic and international obligations incurred by Rover Group and covered by the Varley/Marshall/Joseph (VMJ) assurances was estimated at £1.6 billion at the end of the 1987/88 financial year.

Q12. **HOW REAL WAS THE RISK THAT THESE OBLIGATIONS WOULD IN FACT CRYSTALLISE**

A12. If the Rover Group had suffered a sudden loss of customer and dealer confidence it could have gone into a downward spiral in which it would have been unable to meet its obligations which were far heavier than could have been incurred by a private sector

company in similar circumstances. We believed the risk to be a real one.

para 4 (a) : '(Ministers) ..were also aware of the advice given by Barings..that it was essential to create a competitive market if confidence was to be achieved that the best terms available were obtained.'

Q13. WHAT WERE THE CONSIDERATIONS WHICH LED MINISTERS TO IGNORE BARINGS' ADVICE ?

A13. As noted in the report Barings recognised the Government's right to give consideration to broader considerations, notably the commercial risks to Rover Group of an open auction and the difficulty of reaching a politically acceptable solution by that means.

On the negotiation of the financial terms of the sale

para 5 (a) ' approaches from four other companies ....(which).. were not translated into firm offers.'

(see also Qs 4 and 5. For line to take on individual bidders see Qs 7~~7~~ to 7~~8~~)

Q14. DID THE DEPARTMENT DISCOURAGE THESE ALTERNATIVE BIDDERS IN THE INTEREST OF CONCLUDING A DEAL WITH BAE ?

A14. The companies expressing an interest were neither encouraged nor discouraged, they were simply given factual details of the exclusivity arrangements. None of the companies made anything like a formal bid and no specific price was mentioned by

any of them. >GG ALSO Q5

Q15. WASN'T THE COMPLETION OF THE NEGOTIATIONS WITH BAE WELL BEFORE THE DECLARED END OF THE EXCLUSIVITY PERIOD DESIGNED TO DISCOURAGE OTHER OFFERS ?

A15. No. There was no indication given that a deal with BAe would only be struck at the end of the exclusivity period and anyone with an interest would have taken into account that it was in the interests of all the parties to conclude the negotiations as expeditiously as possible. There was an obvious practical advantage in seeking to conclude the deal if possible in the week before Easter to avoid the complications of the unavailability of Ministers and others over the holiday period.

On the price paid

para 6(a). the consideration of £150m was the most that BAe were prepared to pay.

Q16. HOW CAN THE DEPARTMENT BE CONFIDENT THAT BAE'S DECLARED UNWILLINGNESS TO PAY MORE WAS NOT JUST A NEGOTIATING PLOY ?

A16. Any negotiation involves matters of judgement. We believed there was a very real possibility of BAe walking away from the deal and that the deal struck was the best that could be obtained. The last minute hiatus over the EC conditions indicated that the deal was very marginal for them.

para 6 b. first insert.

(For confidential brief on RG profit projections see Qs 96 and 97)

para 6 (b). second insert.

(for details of the tax benefits see brief 6 and Q & A on Annex 2)

para 6(b). third insert.

(for land values see brief 4 and Qs 50 and 51.For confidential briefing on individual sites see Q & A on annex 3)

Q17. WHY DID THE DEPARTMENT NOT OBTAIN A PROFESSIONAL VALUATION OF THE SURPLUS SITES, ESPECIALLY IN THE LIGHT OF THE NAO REPORT ON THE SALE OF THE ROYAL ORDNANCE FACTORIES ?

(See also Q68)

A17. We did not attempt any valuation of individual assets because we were seeking to sell RG as a going concern. The timing of the disposal of the various sites which might become surplus was not clear at that stage and we believed that none of them had significant disposal value because of the heavy costs associated with disposal. No land gains have yet been realised.

para 6 (b). fourth insert. <u>associated companies.</u>

(See also Q52)

Q18. WHY WAS THE VALUE OF THE HOLDINGS IN ASSOCIATED COMPANIES SO GROSSLY UNDERESTIMATED ?

A18. We and our advisers believed that the aggregate book value of the holdings was in line with the disposal value at that time. Since then special circumstances have applied to the markets in which the two sets of disposals were made. With the passage of

time some of the other valuations contributing to that aggregate now look like overestimates.

para 6 (c). 'the Department could have argued for a price higher than £150 million.'

para 6(d). 'The Departments negotiating resulted in BAE paying£150m for a business which made a pre tax profit of £65m in 1988 and which has surplus assets and other benefits worth at least £250m'

Q19. IN THE LIGHT OF THE ASSET VALUES ESTIMATED BY THE NAO DO YOU NOT AGREE WITH HINDSIGHT THAT A HIGHER PRICE WAS JUSTIFIED?

(See brief 3 and Qs 23, 24 and 47)

A19. No. The value of the Group's net assets was irrelevant to the real value of the company which was what a purchaser was prepared to pay for it as a going concern with its associated risks and opportunities. On that basis we conducted very close negotiations with BAe and arrived at what we are confident was the best deal that could be obtained.

para 6 (c). 'the Department ..could..at least have sought clawback provisions to enable the taxpayer to share in the benefits..

para 6 (d) 'The NAO believes that clawback provisions could have yielded significant benefits for the taxpayer'

Q20. WHY WERE NO CLAWBACK PROVISIONS SOUGHT ?

A20. For two main reasons. In the first place we (and the NAO agree) do not believe that claw back provisions could have been cost free. Second we attached importance to the "clean break" objective.

Remember that BAe were being asked to take on very considerable risks in respect of businesses with a very chequered history. From the outset Bae sought to reduce those risks by pressing for wide-ranging warranties and indemnities from the Government. We were determined that the terms of the deal should not leave the taxpayer with residual but substantial liabilities arising from the normal risks inherent in running the business, particularly as it was a business over which - as a private sector company - we would have no control.

Moreover we sought in negotiation to impose special constraints on BAe:

- in respect of taxation, where trading tax losses were capped at £500m and capital losses and allowances were "ring fenced". The latter restriction was only lifted when it became clear that this was necessary to secure the deal.

- in respect of on-sale, where Bae would face financial penalty if within 5 years it were to dispose of the principal businesses or trade marks without the Secretary of State's consent.

Within these constraints - and having refused to countenance a risk-sharing formula - we were satisfied that the balance of risk and opportunity in the deal was reasonable.

We do not believe that we could have pressed claw-back provisions on BAe without penalty in terms of a reduced consideration or a re-opening of the warranties issue. Nor, on the evidence at the time, did we see the likelihood of windfall gains for BAe over and above what would be needed to fund the business.

If pressed on whether the Government never even considered clawback.

In the context of the on-sale restrictions, consideration was given to more exhaustive coverage of disposal events which could trigger penalty. Such coverage was considered inappropriate; the Government's concern was to prevent on-sale of substantial parts of the business as a going concern and not to impede commercial freedom to manage the business effectively. (See Q36).

On the achievement of the Government's objectives for the sale

para 7 (a) objective..to privatise RG within the lifetime of the current Parliament.

Q21. WAS THERE ANY ADVANTAGE TO THE TAXPAYER IN ADOPTING THIS TIMETABLE ?

A21. This was essentially a political objective but release from the contingent liability of the Varley/Marshall assurances as early as possible was in the taxpayer's interest while a final resolution of the issue of ownership of RG was in the company's best interest. The RG Board agreed the timetable.

para 7(b). 'the best possible terms.'

(see Q 16)

para 7(c) ' certain monitoring obligations

THIS Q/N RELOCATED FROM 23.11 NOTE

Q21a WHAT IS THE COMMISSION MONITORING?

A21a Their State Aid decision makes clear that the six monthly monitoring reports shall cover trading performance, capacity changes, production, pricing policy and intra-Community exports by product as well as a detailed survey of all restructuring measures undertaken in the period.

If pressed In practice I have no doubt that the Commission will focus particularly on the car capacity changes consequential on the closure of Cowley South in the early 90s. Closure of that plant with a capacity of almost a quarter of a million cars is what will remove RG's assembly over-capacity which is what the Commission were particularly concerned about.

Q21b WHAT MUST RG/BAE DO TO AVOID THE COMMISSION DEMANDING REPAYMENT?

A21b The Commission's decision on the Rover case (published in the Official Journal early this year) sets as a condition the "BAe completes the (1988) Corporate Plan.."

From the reasoning set out earlier in the decision it is clear that there are two particular issues of ongoing importance to the Commission*; the first is the overall bill faced by Rover for investment and restructuring over the 5 year Plan period. The commission are interested in this because they look at "aid intensity" - in this case the proportion of that bill represented by the cash injection. Obviously if Rover's capital expenditure turns out higher or lower than forecast that ratio will change. If (for the sake of argument -; I have no reason to believe this will happen) it were significantly reduced then the ratio would increase and Rover would

[* End of VMJ was a 'one-off'.]

have experienced a higher "aid intensity" than the Commission approved. The Commission also compare "aid intensity" with the size of the "counterpart" in prospect. This is basically the benefit to the structure of the EC industry as a whole - in this case from the removal of Rover's excess capacity, which is the second aspect of interest to the Commission. Here the Commission were aware that a reduction of about 30% in car assembly and component capacity was envisaged.

As Members of the Committee will know, the issue of the flexibility available in complying with the Commission's decision was the cause of the last minute delay in sealing a deal. In the event BAe were satisfactorily reassured that within the framework I have described above, they had sufficient management freedom to respond flexibly to market conditions. [No link with matters described in Supp Mem; His was clarificatn not concessn]

para 7(d) 'there was <u>no evidence that the sales negotiations had any adverse effects on RG's performance'</u>

Q22. DOES THIS NOT INDICATE THAT THE DEPARTMENT'S ANXIETY TO PROTECT ROVER GROUP FROM SPECULATION WERE SOMEWHAT EXAGGERATED?

A22. No. There was ample historical evidence of the effect of uncertainty on RG's market share. Fortunately we were able to minimise such uncertainty in the privatisation exercise,mainly by the exclusivity arrangements.

para 9. 'it is important for the Government to <u>establish as realistic a valuation as possible of the undertaking to be sold</u>. (see Brief 3)

Q23. WHY WAS NO DETAILED MERCHANT BANK VALUATION SOUGHT ?

A23. RG's accumulated indebtedness ,poor profit record and high political profile meant that the conventional techniques of valuation were inappropriate. The Group's net asset value is illusory given that it would have gone into receivership years ago were it not for the VMJ assurances; any potential purchaser would take much greater account of its future earnings potential in coming to a valuation and would wish to discount substantially for the uncertainties surrounding the introduction of the new model range and for the restrictions placed by HMG on the future conduct of the business. In practice this meant that the real value of RG could only be established through negotiation.

Q24. IT WOULD APPEAR THAT THE DEPARTMENT WAS SELLING THE COMPANY WITH NO IDEA OF ITS VALUE. IS THIS TRUE ?

A24. RG was so unlike any other business and its future was so subject to uncertainty that it would have been meaningless to think of it as having an absolute value that could be objectively assessed. We were instead trying to establish a fair price for it through a process of negotiation. As a background to that negotiation we kept in mind some benchmarks; the book value of the company, the amounts covered by the Varley/Marshall obligations and the prospects of the company as a going concern.

para 10. ' negotiators should examine the extent (for) <u>providing for the public purse to share in the benefits arising from any subsequent sales'</u>

(See Q 20)

PART 1 : BACKGROUND AND SCOPE OF NAO EXAMINATION

Background

para 1.4. 'consideration by the company and the DTI of various sale options including flotation or placement'

Q25. WHAT ASSESSMENT OF THE PLACEMENT AND FLOTATION OPTIONS WAS CARRIED OUT ?

A25. In 1987 the Chairman of RG was carrying our a detailed study of privatisation options and he submitted an interim memorandum to the Department in october of that year. Following consideration of the memorandum by Whitehall and by DTI advisers RG management proceeded with a study of the option of a placement with institutions,with the assistance of Schroder Wagg,between December 1987 and February 1988. This work was again given detailed consideration by officials and Ministers.

Q26. DID THESE STUDIES SUGGEST THAT PLACEMENT OR FLOTATION WERE FEASIBLE OPTIONS ?

A26. They suggested,as the NAO report notes, that they were dependent on a marked and sustained improvement in the Group's performance which could not be guaranteed in the lifetime of the Parliament.

A placement with institutions followed by a flotation before 1992 was felt by the Government and its advisors to be the only option with any prospect of success if there were no trade sale.There was general agreement in Whitehall that the performance projected in the 1988 Corporate Plan received in December 1987 ruled that option out. The RG study of placement indicated that the institutions would be looking for a return on sales of no less than 6% - a PBIT of £252m - by 1992 if a flotation were to take place in that year. The Corporate Plan projected figures of 4% and £143m and the achievement even of these was subject to considerable uncertainty.

para 1.5 '''exclusive negotiations'

(See Qs 1,2 & 10)

para 1.5. 'a deal was concluded subject to European Commission approval'

Q27. DID THE TERMS ANNOUNCED TO THE HOUSE IN MARCH INCLUDE AN ELEMENT OF PADDING IN ANTICIPATION OF NEGOTIATIONS WITH THE COMMISSION ?

A27. The terms announced to the Houses were those agreed with

BAe and we considered them to represent the best deal that could be agreed at that time. Over the next few months BAe's view of the price it was prepared to pay changed.

para 1.6.and Table 1. ' shows...<u>the taxpayer had provided some £2.9 billion</u> ..to support RG.'

Q28. GIVEN THE ENORMOUS SUMS INVESTED IN RG BY THE TAXPAYER SHOULD YOU NOT HAVE SOUGHT A MUCH MORE SUBSTANTIAL RETURN.?

A28. The Government took the view that the objective should be to look to the future and to relieve the taxpayer of the burden of risks which had resulted in such large and irrecoverable payments. That money is effectively history - swallowed up in the losses of the past.

Objectives of the sale

para 1.8 (a) <u>privatisation within the lifetime of Parliament.</u>

(See Q 21)

para 1.8 (b) <u>Relieve the taxpayer of the liability..(of) ..the Varley /Marshall /Joseph assurances</u>

(See QS 11& 12)

para 1.8 (d) <u>avoid damage to the business</u>

(See Q 10)

PART 2 : NEGOTIATING ARRANGEMENTS

Events leading to exclusive negotiations

para 2.2 'the Rover Group Chairman informed the DTI that he had received an expression of interest' ..

para 2.3 'The Chairman considered that exclusivity would be in the Company's best interest

Q29. WHAT WAS SIR GRAHAM DAY'S ROLE IN THE NEGOTIATIONS AND THE EVENTS LEADING UP TO THEM ?

A29. Sir Graham was asked by Ministers to follow up his initial contact with BAe on behalf of the Government and to assess as quickly as possible whether any early deal was a realistic prospect. Lord Young spoke to Professor Smith to convey the importance that he and his colleagues attached to an early decision.

The negotiations proper were carried out by the Government as shareholder and BAe as purchaser,though the advice of the Rover Group Chairman was sought on matters relating to the conduct and prospects of the business in the course of those negotiations.

[See also brief 1]

PART 3: FINANCIAL TERMS OF THE SALE

February 1988 negotiations

para 3.2. 'Barings advised the DTI that,..a debt free RG could be argued to be worth £950m..but suggested that the..opening position should be... a payment by BAe of £500m.'

Q30. WHY WAS THE CONSIDERATION OF £150m SO MUCH LOWER THAN THE FIGURE SUGGESTED BY BARINGS ?

(See also brief 3 and Q 48)

A30. Barings were suggesting figures on which to open a tough negotiation,not attempting a valuation of the business. The £950m figure was based on assumptions such as the valuation of Austin Rover by a comparison with a greenfield operation of the same capacity and a P/E ratio of 10 for Land Rover, a business needing major capital investment. Barings also pointed out that any purchaser would heavily discount the 'value' of the company because of the uncertainty surrounding its future and a further discount would be applied for the on-sale restrictions imposed by the Government. You will note that,for their part, BAe opened by offering no consideration at all.

para 3.4. 'the Secretary of State and BAe agreed indicative terms.'

Q31. WHAT WAS THE STATUS OF THESE 'INDICATIVE TERMS'?

A31. They were the terms on which both sides agreed that a

deal could be struck if more detailed negotiations established satisfactory mechanisms for payment and for safeguarding the interests of all parties.

Other expressions of interest.

para 3.5. 'four other interested parties'

(See Qs 14 & 15. For confidential briefing on individual bidders see Qs 77 to 80.)

Exclusive negotiations

para 3.6. The department's main concern was the BAe should not sell RG during the first five years of ownership. .....The sale of shares in other businesses or of surplus sites were not covered by these conditions.' (see also brief 7)

Q32. WHY WERE THE ON-SALE RESTRICTIONS IMPOSED?

A32. It was important to give the core business a period of stability unaffected by speculation that it could be quickly sold on to a competitor. The mechanism chosen was to ensure that it was not in BAe's financial interests to sell on the businesses. It also effectively prevents the splitting off and separate on-sale of one of the principal operating subsidiaries.

Q33. ISN'T THE RESTRICTION AN ADMISSION THAT THE BUSINESSES WERE SOLD BELOW THE PRICE THEY MIGHT REACH IN A FREE MARKET ?

A33. A free market auction was rejected because of the risk

of damage to the business. The on-sale restrictions were primarily a policy device to preserve the Group as an independent vehicle producer. One could speculate that prima facie the Group would be worth more to a competitor than as an independent concern or as the subsidiary of a non-competitor; no conclusive evidence exists but, in any case, the Government had wider policy objectives to pursue. Clearly it would have been unacceptable for early on-sale to have taken place in a way that both breached these objectives and resulted in short term profits accruing to BAe.

Q34. WASN'T HMG WORRIED THAT BAE ONLY WANTED THE BUSINESS TO MAKE A QUICK TURN?

A34. Nothing said or done by BAe suggests they wanted the businesses other than to manage them as a successful and long term activity as part of creating a broad-based engineering company.

Q35. IF THE ON-SALE RESTRICTIONS ARE JUSTIFIED WHY DO THEY ONLY APPLY FOR 5 YEARS?

A35. As ministers explained to the SCTI, 5 years was in line with normal commercial time horizons. The intention was to provide a period of stability, not to impose a structure that was immutable indefinitely regardless of developments.

Q36. WHY WAS PROTECTION GIVEN ONLY IN RESPECT OF DISPOSALS OF MAJOR BUSINESSES; WHAT ABOUT THE OTHER ASSETS?

A36. It was no part of the Government's intention to constrain the commercial management of the businesses including' if appropriate the disposal of surplus assets. As emerged in evidence given to the SCTI the great bulk of RG assets are tied up in the

basic operations of the business and could only be realised at the expense of considerable disruption and massive rationalisation and redundancy costs.

Q37. WHY IS THERE NO DEFINITION OF WHAT CONSTITUTED A "SUBSTANTIAL PART" OF AR/LR NOT DEFINED FOR THE PURPOSES OF THE ON-SALE PROVISIONS?

A37. In practice this is likely to be self-evident but ultimately of course the funding agreement could be subject to judicial interpretation or,in the event of dispute about the amount of penalty payable, to expert evaluation by an independent accountant.

Q38. DOES NOT THE SUCCESSFUL NEGOTIATION OF THE ON-SALE RESTRICTIONS INVALIDATE YOUR ARGUMENTS AGAINST THE NEGOTIATION OF CLAWBACK PROVISIONS ?

A38. The two things are quite different. Given RG's importance to the national and regional economy, the Government naturally wished to ensure that the company was not immediately subjected to a further bout of controversy as to its core structure and ownership. On the other hand we did not wish to have a continuing involvement in commercial decisions as to the raising of cash from the disposal of surplus assets and saw no advantage for the taxpayer in doing so,given that BAe would demand some recompense in terms of the consideration for any restriction on its ability to take such decisions

para 3.7. Tax losses

(See brief 6 and Q & A on annex 2)

[Note Qs 72 to 76 deal with the reference. In public discussion of the change in terms say no more than:

The comparison between the terms announced in March and the terms agreed with the Commission in July must take into account the significant and unforeseen improvement in RG's trading performance during the year.]

Q39. WHAT VIEW DID HMG TAKE OF THE COMMISSION'S WHOLE STANCE?

A39. The Commission were there to do their job in enforcing state aids discipline. HMG fully supported that principle but it was our task to convince them of how that principle should apply in the practical circumstances of RG. That necessarily meant at times strong argument over matters like effective debt and the value of the business when we thought the Commission's arguments too theoretical.

para 3.10. Debt write off.

Q40. WHY DID ALL THE DEBT HAVE TO BE ELIMINATED?

A40. It is important to appreciate that RG's debt fluctuates not only according to an annual seasonal trading cycle but also according to the multi-year cycle of major model investment. Because of the impact of tight controls on capital expenditure and borrowing, RG's debt in early 1988 was at an untypically low level. This backlog of capital expenditure, which was required to be made up in order to sustain the longer term commercial position of the company, was planned to unwind over 1988 and 1989 with the

heavy spend on the new K series small engine and the new small and medium size model ranges, R6 and R8.

[**NOT FOR PUBLIC SESSION** Capital expenditure in these two years (at nearly £500m against £260m in 1986 and 7) was projected to contribute to a sharp build up in debt by end 1989.]
Had it not been for its burden of accumulated losses RG could have been expected to approach such a funding trough with a cash surplus arising from the cash in-flow in the period while capital expenditure was low. It was only therefore reasonable for HMG to seek to put RG in a comparable position by at least eliminating all the burden of past losses.

Q41 WHY DID HMG BELIEVE THAT THE ELIGIBLE DEBT FIGURE WAS £800M WHEN THE COMMISSION VIEW WAS THAT IT WAS £330M LESS?

A41 There are four separate components to this:-

(1) the Commission insisted that the Government should not pay off **£100m** of the accumulated debt which must remain on RG's balance sheet.

(2) the differing assessments made of the RG debt build up during the first half of 1988 made by HMG at the onset of the negotiations and by the Commission much later on. HMG put in two components - £50m for debt build up from normal trading and £25m from costs of the LR strike.

In the event the Commission excluded the latter and reduced the former to £25m representing the interest accumulation on the historic debt. HMG recognised this was a "soft" element in the original state aid proposal but saw it as one that could be traded off for a matching reduction in the

consideration.(= reduction of £50m)

(3) The Commission's exclusion of the Wholesale Vehicle Finance element (£155m) from the eligible debt to be paid off. HMG vigorously contested this on the grounds that this was an element of debt just like any other. If RG had not made use of the facility, equivalent bank funding would have been required. We therefore regarded its exclusion as based on academic Commission theology, not economic effect.

(4) Long term accruals. (£25m) These were a component of RG's long term creditors (Ref: Note 17 to the Accounts) but in practice were largely composed of accrued warranty liabilities.

Total reduction = £m 100 + 50 +155 + 25 = £330m

Of course the Commission were prepared to allow the payment of £78m of regional aid making the effective reduction in the injection £253m.

Q42. At the time of original negotiations with BAe (who clearly sought to acquire RG free of debt) what efforts were made to get accurate debt projections for the estimated time of completion?

A42. We obtained from RG at the end of February 1988 their latest month by month calendarisation of total RG debt.

[Following not for public session This showed a figure of £564m for June 1988 but this makes no allowance for the WVF debt nor for the temporary suppression of debt caused by yet-to-be-incurred commercial vehicle restructuring costs. These two factors would give a projection for total effective debt in

excess of £750m.]

Q43. But by looking to write off debt at the mid year wasn't HMG picking up an artificial seasonal peak?

A43. We acknowledge that RG debt does have an element of seasonality with a mid-year peak prior to the key period for car registrations and a further end-year peak. However this cyclical pattern was projected to be submerged in a marked secular trend caused by RG's strong negative cash flow while the backlog on capital expenditure was unwound. Thus the required injection would tend to increase with time.

Q44 It was clear that the paying off of debt was likely to form an important cost in any privatisation of RG: what steps were taken to ensure RG did not artificially boost their debt in this run up to privatisation?

A44. The injection was composed of debt <u>net</u> of cash deposits etc so artificial grossing up would have no effect. Other similar devices would have been exposed by the regular monitoring of the group; as part of this HMG looked closely at all components in RG's balance sheet. Moreover, in recent years HMG had explicitly set borrowings objectives as part of the process of Corporate Plan approvals thus constraining any build up of debt.

Honda agreement with British Aerospace

para 3.12. <u>'Honda were to take a 20% stake in RG'</u>

Q45. DOES THE DEAL WITH HONDA MEAN THAT THE ON-SALE RESTRICTIONS

PROVED INEFFECTIVE ?

A45. No.The on-sale restrictions prevent the sale of a controlling interest in any major RG business and do not prevent the sale of minority holdings.

PART 4 : THE PRICE PAID

para 4.2. 'the sale of the business as a whole'

Q46. WOULD IT NOT HAVE BEEN POSSIBLE TO HAVE GOT A BETTER PRICE BY SELLING THE TWO RG BUSINESSES SEPARATELY ?

A46. The question did not arise at the time. BAe,the only serious bidder, wanted to buy both businesses. The management integration of the two businesses carried out earlier this year indicate the advantages to be exploited by keeping the businesses together.

para 4.3. 'the elements relevant to RG's value'

Q47. WERE THE ELEMENTS LISTED BY THE NAO TAKEN INTO ACCOUNT BY YOU IN PREPARING YOUR NEGOTIATING POSITION ?

(See also brief 3 and Qs 19, 23 and 24)

A47. The book values of assets and the possible value of tax losses were certainly looked at but we did not attempt to value them precisely and then add them up because we did not think, and neither did our advisors, that that was how a purchaser would value the business.

Value of the business as a going concern

para 4.4 'Barings' initial advice to the DTI..'

(See Q 27)

para 4.5 'the European Commission concluded that RG's true value appeared to be about £950m...

Q48. IS IT NOT SIGNIFICANT THAT THE COMMISSION ARRIVED AT ABOUT THE SAME VALUE FOR RG THAT BARINGS DID ?

A48. Not really.In fact the Commission,using a completely different method arrived at a value of about £900m. Some elements in their total were estimates whose origin is unclear. Again the figure represents an extreme negotiating position based on a net book value after a cash injection rather than a realistic valuation of the company as a going concern. Putting a break up value on the company was irrelevant to the deal with BAe. And a break up valuation could in any case only be meaningful if it took into account the costs of break up such as redundancy,as the Secretary of State pointed out.

para 4.5 .'..£150m was consistent with a P/E ratio of 5:1..'

para 4.6 . 'applying the 5:1 P/E ratio to RG;s forecast profit...'

Q49. WAS THE 5:1 RATIO APPROPRIATE FOR RG (eg TOO LOW CONSIDERING ITS RATE OF PROFIT INCREASE) ?

A49. We were not valuing RG by reference to a P/E ratio as it was not relevant to the circumstances of the company or to the sort of sale we were conducting. The Secretary of State cited the P/E ratio to show how different a market valuation was from a break up asset value. The point is that the sort of P/E assigned to a business by the market is much influenced by its past track record as well as its future projections.

It would in any case be very difficult to decide on an appropriate P/E ratio for a company in RG's position. Companies with no established profit record and significant restructuring ahead are subject to modest but widely ranging P/Es.

para 4.7. 'RG's pre tax profit....'

[See Qs 96 & 97 for confidential briefing)

Tax benefits

[See brief 6 and Qs on annex 2]

Value of surplus sites

para4.10. '..no valuation had been carried out..'

Q50. WHY WAS NO UP-TO-DATE VALUATION OF RG'S PROPERTY PORTFOLIO UNDERTAKEN OR THE SCOPE FOR DISPOSING OF SURPLUS ASSETS INVESTIGATED ?

(See briefs 3 & 4 and Q & A on annex 3. NB Discussion of individual sites should take place only in restricted session)

A50. RG was being sold as a going concern with the prospect of production levels being at least sustained. Whilst it is acknowledged that RG had surplus assembly capacity, the fact that it was spread between the 2 main production sites at Cowley and Longbridge meant that there was no early scope for the disposal of discrete land parcels. RG's experience in moving models in mid-life showed the problem of quality deterioration which resulted; this

meant that any rationalisation would only take place as and when permitted by the logistics of model changes. We did not feel that a full revaluation of the sites would have justified the time and expense involved.

paras 4.11 and 4.12. 'Valuation by G L Hearn and Partners..'

Q51. THIS INDEPENDENT VALUATION SHOWS THAT THERE WAS IN FACT SCOPE FOR SPECULATIVE GAINS ON SURPLUS LAND. WITH HINDSIGHT DO YOU NOT AGREE THAT THIS SHOULD HAVE BEEN REFLECTED IN THE PRICE ?

(See briefs 3 & 4 and Q & A on annex 3. NB Discussion of individual sites should take place only in restricted session)

A51. In that we sold RG as a going concern with opportunities and risks that value of disposals was included in the price. I am not convinced that there was scope for such significant gains,over and above the needs of the business for capital, as to justify a separate exercise .

para 4.13 ' No provision for clawback '

(See Q 20)

Values of shareholdings in associated companies

DAF and Istel

para 4.15. 'Barings advised ..that..RG's 40% shareholding in DAF might be worth £40-50m..following flotation..a total value of £147m..'

para 4.17 'RG have sold their holding in Istel for £38.6m compared to Barings estimate of £8-10m'

Q52. HOW DID THE VALUE OF THE DAF AND ISTEL SHAREHOLDINGS COME TO BE SO GROSSLY UNDERESTIMATED ? (see also Q104)

A52. The original valuations were quite reasonable at the time. As the NAO notes (para 4.16)the increase in the value of the DAF holding reflects changes in the truck market, which underwent a boom that was quite unexpected by industry experts, as well as DAF's performance within it . The increase in the value of Istel was also quite unforeseen by experts.

NAO Conclusions

para 4.18 NAO valuation :

insert (a) £140m on the basis of profits

(See Qs 96 & 97 for confidential briefing)

insert (b) £33-40m tax losses

(See brief 6 and Q & A on annex 2)

insert (c) £33.5m for surplus sites

(See brief 4 and Q & A on annex 3)

para4.18 'the NAO assess the total value of RG to have been at least £206.5m at the date of sale..

para 4.19 'the NAO conclude that the sale price of £150m fell significantly short of the real value..

(See brief 3 and Qs 23, 24 and 47)

PART 5 : ACHIEVEMENT OF THE GOVERNMENT'S OBJECTIVES

(a) To privatise Rover Group within the lifetime of the current Parliament. (para 5.2)

(See Q 21)

(b) To relieve the taxpayer of the liability represented by the Varley/Marshall/Joseph assurances.. (paras 5.3 -6)

(See Qs 11 and 12 and background note 12)

...while securing the best possible terms for the sale of the Rover Group. (para5.6)

(See Qs 16 & 19)

(c) To achieve a clean break without further risk to the taxpayer.

(Not controversial)

(d) To avoid damage to the Rover Group through privatisation.

(See Q 10)

Q and As on ANNEXES

ANNEX 1 - (see background note in Brief 2) -SEQUENCE OF FINANCIAL TERMS PROPOSED

Q53. WHY WERE THE MARCH CONDITIONAL TERMS SO MUCH MORE GENEROUS THAN THE FINAL TERMS SANCTIONED BY THE EC?

A53. The final terms reflected long and detailed negotiations during which the perceptions of the vehicles market and Rover's performance had significantly improved. There is no reason to believe the July terms could have been negotiated with BAe in March. (NB reference to additional concessions NOT to be made in public session).

Q54 WITH HINDSIGHT DO YOU THINK THAT THE DEPARTMENT COULD HAVE NEGOTIATED A BETTER DEAL IN MARCH?

A54 Any negotiation involves matters of judgement. We believed there was a very real possibility of BAe walking away from the deal and that the terms offered in March were the best that could be achieved at the time.

Q55 WHY DID BAe ACCEPT A £250M REDUCTION IN THE CASH INJECTION ONLY THREE MONTHS LATER?

A55 Events showed how close to walking away BAe were. The unringfencing of the capital tax losses and allowances offset the reduction but clearly the improvement in RG's trading performance and the strength of the market over the period were the vital factors.

Q56 DID THE TERMS ANNOUNCED TO THE HOUSE IN MARCH INCLUDE ELEMENT OF PADDING IN ANTICIPATION OF NEGOTIATIONS WITH THE COMMISSION?

A56 The terms announced to the Houses were those agreed with BAe.

ANNEX 2 (see also background note in Brief 6) - TAX

Q57. WHY DIDN'T DEPARTMENT DO THIS SORT OF DETAILED VALUATION AT THE TIME?

A57 Significant resources were put into tax matters and the Department used a tax partner and staff of Slaughter and May in this area. Valuing tax losses is not an exact science and I do not believe there is anything here to suggest this was an area in which additional time and resources would have yielded a benefit.

Q58 SHOULDN'T DEPARTMENT HAVE APPOINTED SPECIALIST TAX ADVISERS MUCH EARLIER?

A58 General advice was available from Barings. Specific advice could only be formulated once one was in a situation of a specific disposal option in which the tax status of the ac~~en~~quirer was known.

Para 2.1.1

Q59 WHY WERE RG'S TRADING TAX LOSSES CUT BACK TO £500m - WHAT WAS BASIS FOR THE FIGURE

A59 In view of the fact that HMG was injecting cash to reduce the debt caused by historic losses, it was not considered right that RG should have the full tax benefit of those losses as well. The £500m figure was simply the result of negotiation; it had no special logic beyond the commercial one of being the figure that both sides were willing to accept as part of the total package.

Q60 ISN'T IT TRUE THAT IT WAS NOT ACTUALLY FEASIBLE FOR RG TO USE

MORE THAN £500m OF TAX LOSSES?

A60 Important point for Government was to ensure that they couldn't use the excess even if their profitability were to accelerate rapidly.

Para 2.2

Q61 WHY WAS THE RING-FENCE LIFTED ON CAPITAL LOSSES/ALLOWANCES

A61 This was a deliberate move to ease the impact of the cut in the cash injection. Unlike the trading tax losses which were effectively ringfenced by the 'same trade' provisions of tax legislation, the ringfencing of capital losses/allowances was a negotiated restriction under the terms of the March conditional agreement. Lifting the ringfencing just restored the position under normal tax law.

If pressed on the fact that ringfencing was described to SCTI as plugging a significant loophole

The 'loophole' is a normal feature of the tax law. Originally we intended to restrict the use which could be made of the capital allowances and capital losses as part of the terms of the March conditional agreement. But we decided to concede the dropping of this restriction as part of the renegotiation.

Para 3.1.3

Q62 BUT WON'T THE TRADING TAX LOSSES STILL HAVE A USE BEYOND FIVE YEARS

A62 This is correct but discounting back means that the present value is small. Beyond five years of course financial projections which will determine tax loss utilisation become very uncertain.

Para 3.1.5

Q63 **WHY SUCH A HEAVY DISCOUNT?**

A63 Valuing tax losses is subject to many uncertainties and I am not at all surprised that TR should consider such a discount appropriate. Unless there is a clear and quick route for a purchaser to use the tax losses of a company bought (manifestly not the case here), the value attributed to them is always very heavily discounted.

Para 3.2

Q64 **BAe CLEARLY HAVE SITES TO DEVELOP; SURELY A NIL VALUE FOR RG'S CAPITAL LOSSES IS UNREASONABLE AS THEY COULD OFFSET FUTURE PROPERTY GAINS?**

A64 It is just very difficult to value tax losses. Touche Ross arrived at a nil value, other experts might have said something different.

Para 4.1/4.2/5.2

Q65 **WHY NO BENEFIT SHARING ARRANGEMENT?**

A65 Such an arrangement would have added considerable complexity and been incompatible with the whole "clean break" approach of the deal. Sharing of tax benefits is I understand most unusual; while I agree that the size of the tax losses and allowances in RG's case is itself unusual, I do not believe that would have been a sufficient reason to depart from the "clean break" approach.

ANNEX 3 - (see also background note in Brief 4) - LAND VALUE

(NB No reference to specific sites except Bathgate to be made in public session; for this reason other site[specific Q/As are located in supplementary memorandum section Q98-103).

Para 4.1

Q66 SURELY THIS IS AN ABSURDLY LOW VALUE WHEN COWLEY SOUTH ALONE COULD SUPPORT A HUGE COMMERCIAL REDEVELOPMENT?

A66 This is the figure arrived at by professional valuers using conventional techniques. Even so it largely neglects the costs associated with making sites available for disposal. There is no huge property windfall to be made; I do not believe it was ever part of BAe's rationale for buying the business and these figures bear that out.

Para 4.2

Q67 WHY IS APPENDIX 2 WITHHELD?

A67 This contains commercially confidential information.

General

Q68 WHY DIDN'T THE DEPARTMENT ITSELF DO MORE WORK ON VALUING POTENTIAL LAND GAINS,[ESPECIALLY GIVEN THE ROF CONTROVERSY]?

A68 RG, with the exception of Bathgate, did not have vacant land. While some rationalisation in the nineties was likely given RG's over-capacity, the precise scope and timing was uncertain. Disposal gains were not seen as material in relation to the overall business, its risks and its cashflow, and those were the important factors in the sale. [The PAC did not publish their report on ROFs until October 1988.]

(See background note 15 on ROFs).

If, pressed on subsequent BAe revaluation

The sale of RG was a negotiation about the overall business taking into account its opportunities and risks; it was not a sale based on book value of assets - let alone any particular class of asset. Revision of the accounting value of assets does not affect their real earnings potential in terms of cash generation, and that is what matters in an acquisition. Revaluation is of relevance to BAe for the quite separate reason that it afects their gearing and hence ability for and cost of borrowing funds.

Q69 **DOES NOT BATHGATE SHOW THE SCOPE FOR SPECULATIVE GAINS IN WHICH THE TAXPAYER WILL NOW MISS OUT?**

A69 Bathgate is a special situation in that it represents a facility that has been out of use for a number of years. However with the subsequent refusal of planning permission, its value is minimal. Even if planning consent had been obtained, the proceeds -probably in the form of royalties from site rentals - would have been modest. And to realise such proceeds, RG would have had to incur financing andother development costs. Given the uncertainties at the time any purchaser of RG would naturally have heavily discounted the prospect of significant proceeds from the site.

NB All discussion of individual sites except Bathgate to take place in restricted session.

Q70 WHY WAS NO PROVISION BUILT INTO THE BAE CONTRACT FOR THE TAXPAYER TO SHARE IN ANY PROPERTY GAINS?

A70 Believe there are 2 arguments against this:-

(i) the first was Ministers' policy objective of a "clean break". Otherwise HMG would be sucked into the very process of disposals. This could give rise to potential for conflict between the taxpayers' interests under any such clawback clause and pure commercial arguments. This could compromise the very commercial freedom and market disciplines which privatisation was to achieve.

(ii) the second argument applies equally to <u>any</u> suggestions of the consideration being performance or profit related; it would not be cost-free. BAe was being asked to take on considerable risks. If the upside potential for them were to have been limited in some way, one can be absolutely sure they would have pushed down the fixed component of the consideration. That would be fully justified. The profit-related element would not, therefore, just be added to the £150m specified in the actual sale contract. The end result would have been to return some of the risk to the taxpayer.

Q71 INTERPLAY BETWEEN SCOPE FOR PROPERTY GAINS AND THE TERMS OF THE AGREEMENT ON TAX, ESPECIALLY THE COST OF UNRING-FENCING?

A71 The scope for the use of capital losses to offset tax liaibility on property gains under the <u>July</u> agreement is

Q AND As ON SUPPLEMENTARY MEMORANDUM

Background note in Brief 9 covers disclosure issues

General

Q72 WHY WAS THE GOVERNMENT SO INTENT ON DOING THE DEAL THAT IT WAS PREPARED TO MISLEAD PARLIAMENT AND HOODWINK THE COMMISSION?

A72 The background was that BAe were poised to walk away from the deal if they did not obtain additional concessions. The last minute hiatus over the deal is evidence that, even with such concessions, the deal was highly marginal for them and I do not believe they were bluffing when they insisted on them. If the deal had collapsed Rover would have been exposed to damaging uncertainty in the run up to the key registration period. The uncertainty would have been compounded by the unclear intentions of trade bidders and the fact that a placement/flotation alternative would have taken time to work up. In such a situation confidence could have evaporated fast - possibly to the extent that creditors would be so shaken by events that they demanded formal guarantees or an immediate injection of cash, both of which could have been blocked by the EC. That uncertainty would have been deeply damaging to Rover, its employees suppliers and dealers and, potentially through the VMJ assurances, to the taxpayer. The Government therefore sought a way through by offering a package of concessions on separate matters which we believed to be consistent with the terms of the Commission's approval as they did not affect the competitiveness of Rover's production. They were not notified to the Commission because we were anxious to avoid any further delays which might put the precarious deal at risk. The Government was scrupulous to

precisely that afforded under general tax law and practice. The decision to unring-fence capital losses was a deliberate policy move to offset the reduction in the capital injection being imposed by the EC Commission.

observe the proprieties through what it said about the terms in the supplementary estimates and elsewhere, even though this meant opening itself up to possible questions. In the event such questions were not raised. This approach was followed through in disclosing the BAe costs payment in the Industrial Development Act Report this year. Of course the Government fully recognised that the concessions were material to the PAC investigation and volunteered details to the NAO at the earliest opportunity so that Parliament, through the PAC, was fully informed.

Q72a WILL THE DEPARTMENT NOW PUBLISH ALL THE DOCUMENTS RELATING TO THE PRIVATISATION?

A72a I see no need to do so. The very copious documentation has been made fully available to the NAO and their report and memorandum give the whole picture.

Q72 WHEN HMG BOASTS OF ITS CLEAN RECORD ON STATE AID, ISN'T THE PACKAGE OF HIDDEN CONCESSIONS EVIDENCE OF SHABBY DECEIT?

A72 There is no doubt that we strongly support the control of state aids. Because of the risk of losing this deal with BAe with all the attendant commercial damage that would have caused to Rover ,HMG sought to find additional concessions to bridge the gap which it believed were consistent with the terms of the Comission's approval.

Q73 WON'T THE COMMISSION NOW CHALLENGE THE PACKAGE AND DEMAND REPAYMENT?

A73 We have made it clear that we will co-operate fully with any enquiries which the commission wishes to make. It is far too early to speculate on the outcome of that process.

Q74 SO DOES THE UK AGREE WITH THE COMMISSION TAKING A TOUGH LINE ON RENAULT? DUAL STANDARDS?

A74 Two cases quite separate. The whole basis for the Commission approving the Renault case hinged on the transformation of the status of that company and the restructuring of capacity offered at the time. Up to the Commission to determine whether those conditions are being realised. What we are discussing here is some marginal concessions to BAe which we believed were consistent with the original terms of the approval.

Q75 WERE ANY HINTS GIVEN TO THE COMMISSION ABOUT THESE CONCESSIONS? IF NOT, WAS IT NOT AN EXTRAORDINARY RISK FOR HMG TO TAKE?

A75 Privately some indication was given to the Commission that the Government might seek to assist with BAe's costs in buying out the minority whose existence was clearly an anomaly not of their making. The Commission had also indicated sympathy for additional assistance to BAe outside the vehicles sphere in which it feels it necessary to police state aids particularly rigorously. However, they could of course give no assurance as to their attitude if such actions subsequently were drawn formally to their attention. HMG was faced with an exceptional situation in which the alternative would be to jeopardise the business of a vital exporter, employer and purchaser of components and services

Q76 WHY THE SECRECY OVER COMPANIES EXPRESSING AN INTEREST IN RG WHEN THERE WAS SPECULATION BEFORE THE LEAK?

A76 I believe it is one thing for there to be press speculation but quite another for the Department publicly to disclose approaches made to it in confidence. Until the end of last week I was not aware of speculation going beyond Ford and Volkswagen.

EXTRA MATERIAL ON OTHER EXPRESSIONS OF INT.

Para 2

Q76A HOW FAR DID VW GET IN NEGOTIATIONS WITH RG/HMG BEFORE BAE MADE THEIR APPROACH?

A76A In 1987 the focus for exploring options lay with Graham Day and his Board. We were not a party to the very preliminary exploratory talks which Rover held with VW though there was, around that time, some contact between Ministers and VW to discuss the company's purchasing of UK components. In the course of those discussions VW's interest in Rover was certainly mentioned but neither as a result of those contacts nor, more importantly, as a result of the RG/VW discussions did matters reach the stage at which there was a specific package on which HMG was required to take a view.Following the BAe announcement about BAe VW wrote to the Department in very general terms about their interest; this was replied to along lines common to the letters to the three other companies expressing interest at that time.

Q76b WHAT WAS THE POSITION WITH FORD AT THE TIME OF PRIVATISATION?

A76b Ford had not launched an approach to HMG to acquire Rover since negotiations were broken off in 1986.

<u>If pressed on whether Ford would have made an offer if there had not been the exclusivity arrangement.</u>

That is hypothetical. [One can speculate that, if there had been an open auction particularly with any prospect of Rover being sold to one of Ford's rivals, Ford would have made a bid, though probably not for the business as a whole]

Q77 WHY DID TOYOTA WANT TO BUY RG IF IT WAS HATCHING ITS GREENFIELD APPROACH?

A77 There was no direct contact in 1988 between the Department and Toyota over this matter. They were simply identified by Lonrho as their partner within the industry in the context of this interest in RG.We have recently contacted Toyota who told us that they had not in fact had any had any dealings with Lonhro on this matter.

Q78 WHO WERE MELTON MEDES? WERE THEY A CREDIBLE PURCHASER?

A78 That company is a relatively small East Midlands based engineering group. It would be wrong of me to comment on its credibility as a purchaser of RG since, as matters were not pursued by them, the Department had no cause to investigate

it. Of course the difference in respective sizes of Melton Medes and Rover is readily apparent and, on the face of it, it would seem preferable for RG to form part of a group with wide resources.

Q78a BUT DIDN'T MELTON MEDES APPROACH THE DEPARTMENT IN 1987 BEFORE THE EXCLUSIVITY ARRANGEMENT CAME INTO FORCE? WHY DIDN'T YOU INVESTIGATE THEN?

A78A In 1987 potential trade bidders were being looked at by Graham Day and his Board as part of their review of options for the company. Their approach was therefore referred to RG.

Q78b IF THE MELTON MEDES AND VW APPROACHES IN 1987 WERE REFERRED TO DAY FOR HIS REVIEW OF OPTIONS, WHY THE QUITE DIFFERENT APPROACH WHEN BAE CAME ON THE SCENE?

A78b Graham Day's review of options was known publicly and any approaches at that time were simply referred to him. At the time of the review Sir Graham explained to Ministers that opportunities for sale of the group to a single purchaser might have to be pursued single mindedly within a limited window of opportunity. Trying to evaluate any such option against every other possibility would lead to the very auction the Board was so anxious to avoid. When the BAe approach occurred Sir Graham told Ministers that here was a particular opportunity to privatise the Group while preserving the independent existence of the core businesses and at the same time giving them access to the wider resources of a large engineering group. Ministers had to weigh up whether it was right in those circumstances to grant BAe exclusive negotiations to see whether acceptable terms could be reached, or risk losing this particular opportunity of privatising the Group in a way that would

not generate the controversy experienced in 1986. In the event they chose to grant a limited exclusivity period of two months.

Q79 WAS IT THE CASE THAT ALL THE INTERESTED COMPANIES WERE DISCOURAGED FROM TURNING THEIR EXPRESSIONS OF INTEREST INTO FIRM OFFERS?

A79 As the Secretary of State explained to the SCTI these firms were neither encouraged nor discouraged. They were simply told the facts of the decision to negotiate exclusively with BAe for a limited period.

Q80 BUT WEREN'T FORD QUIETLY WARNED OFF?

A80 Ford would have been well aware that it could have made an offer; exclusivity was effectively a declaration of intent about the negotiating process only.

<u>If pressed</u>

I have no doubt that Ford put resources into carefully reading the political climate in all sorts of ways. They had reason to be wary after the events of 1986 and since that time had clearly not been prepared to move for RG without being invited to do so.

<u>If pressed on whether Departmental officials had any contact with Ford at this time in which acquisition of RG was discussed (beyond the formal exchange of letters)</u>

Ford naturally maintain contacts with the Department of various levels. They would probably have interpreted the lack of any overture to them as a rebuff.

<u>Para 3a</u>

Q81 WHAT WERE BAe's ACQUISITION COSTS?

A81 The major cost in this context was the costs of buying out the minority shareholders (which at £1 per share was equivalent to about £13m) but BAe also faced significant merchant banking and legal advice fees. There was a schedule of these categories of costs and the Department undertook to pay up to £9 $^{1}/_{2}$m in respect of them once BAe submitted a claim showing the expenses incurred. In the event their claim was fully covered by the costs of the minority purchase.

Q82 WHY WAS BAe EXPENSES GRANT SET AT 9.5m? TO AVOID PARLIAMENTARY SCRUTINY?

A82 This was a negotiated figure.

<u>If pressed</u>

Both we and BAe were aware that a grant above £10m would have required an immediate affirmative resolution rather than simply being reported (as it subsequently was in this case) to Parliament through the annual Industrial Development Act report.

Q83 WHY DIDN'T HMG BUY OUT THE MINORITY AND THEN SELL ALL THE EQUITY TO BAe?

A83 This would have had two disadvantages:

(a) it would have been time-consuming when it was in everybody's interests to get the sale to BAe completed so that RG could get on with normal commercial life;

(b) it would have directly associated HMG with the buy-out price to the minority in a way that would have been bound

to be contentious; under the mechanism actually used the price was that set as "fair and reasonable" by RG and BAe and their advisers. Because the grant was capped HMG was detached from the price setting process.

Q84 HOW WAS GRANT PAID? LEGAL BASIS?

A84 The money was paid under Section 8 of the Industrial Development Act. The Department took the view that a single grant under the Act could be paid in connection with the deal, since (by making the transaction happen) it was fulfilling the purposes set out in the Act.

Para 3b **(RG cost reimbursement)**

Q85 MECHANISM, AUTHORITY, RATIONALE ?

A85 The money was reimbursed to RG against documentary evidence of the bills paid. The authority to pay was the ambit of the revised Supplementary Estimate laid before Parliament. The Department's legal advice was that it was absolutely proper for it to pay RG's costs.

Q86 WAS SUPPLEMENTARY ESTIMATE MISLEADING IN NOT IDENTIFYING RG'S COSTS SEPARATELY

A86 The text of the revised supplementary estimate referred simply to "privatisation expenses : expenses in respect of Rover Group's return to private ownership." This had been deliberately and properly changed from the previous version which had the heading "Advice to the Department" and, at the same time, the amount was increased from £300,000 to £1.8m.

Given that it was after all the Government's privatisation policy which was leading RG to incur these costs I do not believe it is wrong to lump together the costs incurred both by HMG directly and through RG.

If pressed In terms of strict financial transparency I agree there is an argument for separate quantification but I repeat that it was HMG which caused RG to incur these costs; in that sense they were no different from costs borne direct by the Department.

Para 3c (Deferment)

Q87 DID SOS MISLEAD WHEN REFERRING TO FINAL RESOLUTION OF TAX MATTERS? ISN'T THE TRUTH THAT THERE WAS A CLEAR AGREEMENT TO DEFER UNTIL MARCH 1990?

A87 The precise mechanism for the deferral is that payment may be triggered either by a tax event or by the long stop date of 31 March 1990 - whichever is the sooner. The tax event is however within the ability of BAe to control so that it must be likely that it is the long stop date which will in practice act as the trigger; it was the intention of the parties that this should be so.

If pressed on why the statement did not simply refer to an 18 month deferral

The deferral mechanism and its description had to take account of the background of the State Aid case. It is possible that announcement of a straight deferment would have been investigated by the Commission though we would argue that it was a benefit to BAe not RG. We did change the supplementary estimate to indicate, that matters had changed from a straightforward receipt in 1988/9.

Q87a WHAT WERE THE TAX MATTERS THAT HAD TO BE RESOLVED?

A87a These concerned the provisions in tax law under which, following a change of ownership, fundamental reorganisation of their operations can lead to a company losing the whole of their accumulated tax losses [Section 768 of the Income and Corporation Taxes Act 1988]. BAe needed to know how much flexibility they had without risking challenge under those provisions. Specific ideas and Inland Revenue decisions on them would necessarily take time but the delay in payment of the consideration could not go beyond 31 March 1990.

Q87b ISN'T IT UNUSUAL FOR THE IR TO GIVE PRE-CLEARANCE?

A87b That is correct but in this case it was in the public interest that they should do so. The certainty that it would give to BAE would enable them to make the best use of the RG tax losses and this was reflected in the sale terms.

Q88 ISN'T £22m AN UNDERESTIMATE OF THE VALUE OF THIS CONCESSION GIVEN INTEREST RATES?

A88 No, because the increase in interest rates is offset by the increase in tax paid by BAe on its profits. Our most recent accountancy calculation shows the net cost of deferment to be £22.5m.

Q89 IS THE DEPARTMENT SURE IT WILL RECEIVE THE CASH ON TIME?

A89 BAe are a blue-chip company of the utmost reputation and I am sure they would be surprised that such a question was being asked.

Para 3d

Q90 DOES THE ACCOUNTING OFFICER BELIEVE IT IS GOOD FINANCIAL OR ADMINISTRATIVE PRACTICE TO LINK ONE ASPECT OF BAe's DEALINGS WITH GOVERNMENT (COLUMBUS) WITH SOMETHING (RG ACQUISITION) IN QUITE ANOTHER SPHERE?

A90 In general I would agree that it is desirable that "Chinese Walls" should apply not least in the interests of financial transparency. However one has to recognise that the circumstances were exceptional in that HMG faced a situation in which a deal which it believed was in the national interest might fold, thereby exposing RG to a renewed bout of uncertainty which would have been immensely commercially damaging to itself and potentially - through the Varley Marshal assurances - to the Taxpayer.

Q91 WHY HAS THE FACT THAT BAe WILL NOT HONOUR THEIR EARLIER COLUMBUS OFFER NOT BEEN REPORTED TO PARLIAMENT?

A91 The design configuration for the polar platform has undergone considerable modification since discussions with industry were first opened. We are discussing a new configuration with industry and the industrial contribution will depend on the configuration that eventually emerges.

Q91A BUT THE MEMORANDUM SAYS THE £5M <u>WILL</u> NOW BE PAID BY THE DTI

A91a That was the position anticipated at the time. We are now discussing a different project with different costs and an industrial contribution is being sought from, among others,

BAe.

Q92 IF THE COMMISSION HAD HINTED THAT ADDITIONAL AID FOR BAe IN ANOTHER SPHERE WOULD BE ALRIGHT, WHY DIDN'T HMG DISCLOSE IT AT THE TIME?

A92 I think it most unlikely that the Commission would have looked favourably on something that was deliberately and simultaneously portrayed as offsetting their action on the RG case. At most all they were hinting at was that in the course of normal business HMG had many dealings with BAe which might offer some scope for flexibility.

Q93 WASN'T HMG'S REAL CONCERN THAT ACKNOWLEDGING THE COLUMBUS ELEMENT WOULD COMPROMISE THE LINE THAT RELATIONS WITH BAe ON RG HAD BEEN KEPT SEPARATE FROM OTHER ISSUES.

A93 Important point was that there had been no additional commitment in the major areas of Launch Aid or procurement.

Para 4

Q94 DOESN'T THE SIZE OF THE ADDITIONAL PACKAGE SHOW HOW DISINGENUOUS WAS THE STATEMENT DESCRIBING THE FINAL SALE TERMS?

A94 The text of the statement was the result of Ministerial deliberation. Ministers were of course attacked over the apparent discrepancy between the indicative terms described at the end of March and the final post-EC terms; it would thus have been in their own interests to describe the additional concessions if need to finalise the deal quickly had permitted.

Q95 WHOLE EPISODE SHOWS WILLINGNESS OF HMG TO BE ECONOMICAL WITH

THE TRUTH AT HOME AND TWO-FACED IN ITS DEALINGS ABROAD?

A95 I believe that is a tendentious description of a very difficult situation. This was a position in which the alternative of the deal collapsing would have been very damaging to RG whose interest lay in speedy resolution of the privatisation issue.

Para 6

Q96 **DOESN'T THE TABLE SHOW BAe WERE BUYING A STRONG BUSINESS WITH GOOD PROFIT POTENTIAL? WOULDN'T THIS ALONE JUSTIFY RATHER MORE THAN £150M?**

A96 This table cannot be read in isolation from the text below it. RG is of course a business with a turnover of over £3bn. I am sure this Committee would agree that, although the profit trend is basically in the right direction, it is nowhere near the absolute level appropriate to a business of this size. From BAe's point of view they were taking on considerable risks - of which the most significant internal and external ones are listed. Moreover because of the constraints imposed by the on-sale clauses and the terms of the EC approval relating to capital expenditure, their room for manoeuvre was constrained. It is clear that BAe faced a considerable task in convincing commentators and others that this was a desirable strategic move to make. Only history will tell if their judgement was right but I do not believe this Committee should underestimate the very real risks that they were taking on; they are precisely the sorts of risks which any prudent purchaser will discount for.

Q97 **BUT 1988 PROFIT SUGGESTS FIGURES WERE VERY CONSERVATIVE; THE DISCOUNTING WAS ALREADY BUILT-IN TO THE PROFIT TRENDS?**

A97 The market conditions in 1988 were much more favourable than any commentator would have forecast at the beginning of that year. The strength of that market naturally translated into better profit margins even though in volume terms RG were really only marking time. As history shows, when competitive pressures re-emerge, the car market can become a very expensive place to be as every manufacturer seeks to keep volume moving by incentives to dealers etc. Of course RG hope that their market repositioning will sustain their profit margins in such conditions; again that is an as yet unproven factor and any purchaser would see it in that light.

Para 8

Q98 DOES INCLUSION OF DREWS LANE MEAN RG PLAN TO CLOSE THAT PLANT?

A That is a matter for Rover Group, but I would draw Member's attention to Sir Graham Day's reply to the SCTI last November when he noted the eventual intention to consolidate at Longbridge or Gaydon activities which currently take place at Drew's Lane. He has explained that one of these activities is engine manufacture, as a natural consequence of the displacement of the A-series by Rover's new K-series engine manufactured at Longbridge.

Q99 HOW DID NAO KNOW TO INCLUDE IT IN THE CONSULTANTS TERMS OF REFERENCE? IS CLOSURE MENTIONED IN DEPARTMENTAL PAPERS AT THE TIME OF THE BAe DEAL?

A99 I believe Sir Graham Day's reply to the SCTI last November makes it an obvious assumption that the plant will close at some point. If pressed Yes, our working assumption at the time

was that Drews Lane would close at some undetermined date.

Q100 COWLEY NORTH TO BE CLOSED AS WELL?

A100 Rover have said that Cowley is and will be their centre for executive car production and they have recently announced investment in the Body Plant site for that range. They have acknowledged that consolidation within the site is likely to mean the North Works will not be required for vehicle manufacture.

Q100a SO THE NAO VALUATION OF SURPLUS SITES IS ALREADY TOO LOW?

A100a It is premature to <u>assume</u> disposal of the North Works site but I would agree that, if Hearns had been asked to repeat the exercise today it would be only sensible to include the North site.

<u>If pressed on value</u>

With the same methodology Hearns would, I expect, arrive at a figure comparable to that reached for the South site which is slightly larger in area.

Q101 WHAT ABOUT THE OTHER FORMER COMMERCIAL VEHICLE SITES TO BE CLOSED?

A101 The land and buildings of the <u>Leyland engine plant</u> have already been transferred to Leyland-DAF as part of the 1987 agreement between RG and DAF. The <u>Leyland foundry building and land</u> sold separately following closure. The <u>Scammell plant</u> is likely to be retained by RG and leased out piecemeal for several years until the local planning situation is

clarified after the construction of a new road in the area. There are no imminent plans for disposal.

Q102 DOES NOT COWLEY SOUTH OFFER SCOPE FOR RE-DEVELOPMENT AT GREAT PROFIT FOR A COMBINATION OF DISTRIBUTION/RETAIL/HOUSING AND EXPLOITING THE SOON TO BE EXTENDED M40?

A102 Plans for Cowley South are at a very early stage; RG are only beginning to discuss some of the options with local interests and the timing remains uncertain. Because of interlinking with the other Cowley facilities there will be further costs to be incurred. The site is of course still some way from the proposed Motorway extension.

Q103 WHAT ABOUT LLANELLI?

A103 Residual business at Llanelli (after transfer of the pressings work to Swindon) has now been sold to Camford as a whole; no property gain at all.

Para 9

Q104 BARINGS' VALUATION HAS PROVED HOPELESSLY LOW ON DAF AND ISTEL. ISN'T IT THE CASE THAT THEIRS WAS A SIMPLISTIC APPROACH WHICH RESULTED IN A MASSIVE LOSS TO THE TAXPAYER?

A104 As the text makes clear one element of Barings' calculation, LR Santana, resulted in what is almost certainly a substantial over-estimate of disposal value. In the case of ARCONA RG have since bought out the other partner at considerable cost but until the business recovers, it is most doubtful whether the now 100 per cent stake is worth <u>any</u> positive sum. Barings were not asked to do a full and detailed valuation of each

stake; that said I believe that their conclusions at the time were fully justified. In the case of DAF and ISTEL the market conditions and perceptions of the companies clearly strengthened in the period after the sale to BAe. But that is simply hindsight and not something which could influence perceived value at the time.

Extra material on DAF

At the time of privatisation specialist professional commentators were forecasting only minor growth or an actual fall in the commercial vehicle market. In November 1988 the Economist Intelligence Unit was forecasting a continuing drop in registrations into the early 1990s. In the event this highly volatile market became extremely buoyant and in 1988 CV production in the UK increased by almost 29% to reach the highest level since the 1980 boom. This growth was paralleled in the rest of Europe in a way that exceeded the industry's wildest expectations. The Chairman of DAF was recently quoted as saying that DAF's performance had exceeded what could have reasonably been expected at the time of the merger.

Extra material on Istel

Istel had been the subject of a management buy-out through a competitive process in late 1986 and the sale completed in June 1987. At that time the MBO's terms were the best, ahead of the only other firm offer on the table. There was nothing whatever to suggest the prospect of trade buyer interest at much higher prices. As a result of RG's retained stake following the MBO, they had representation on the Istel Board. Up to the time of theBAe deal

there was no information to Government from this source or any other to suggest the sort of final price which that stake eventually realised. That was in a sale to one company which in a strong market clearly particularly valued it as complementary to its existing operations.

CLAWBACK PROVISIONS IN RECENT PRIVATISATIONS

Short Bros and Harland and Wolff

1. Short's has one main disposable asset, its airport, which is subject to a ten year clawback period during which any proceeds from disposal must be shared with the taxpayer. The company's military business is also protected against disposal for ten years. Harland and Wolff's sites in Belfast are subject to clawback provisions on the same terms as the airport.

2. All the clawback arrangements contain "earn out " provisions whereby the Secretary of State undertakes to look sympathetically at any disposal the proceeds of which are re-invested in the development of the business.

Water

NB. NOTHING SHOULD BE SAID ABOUT WATER PRIVATISATION DURING THE CURRENT OFFER PERIOD.

3. Surplus land belonging to the water businesses is valued as at end March 1989 with a discount taking into account the need to obtain planning permission. The value of the land, and any proceeds from disposal, feed into the projection of future income which is made when setting prices to ensure a return for the shareholders . Prices will rise by the RPI plus a "K factor" which is set by City advisors. If any disposal earns more than the site concerned was valued at then half the excess is returned to the consumer in the form of a reduction of the K factor.

ROVER GROUP CAR PRODUCTION AND REGISTRATIONS

	1980	1981	1982	1983	1984	1985	1986	1987	1988	Ytd Aug 88	Ytd Aug 89.	Ytd Oct 88	Ytd Oct 89
Total UK Car Production.	923744	954650	887679	1044597	908906	1047973	1019519	1143045	1226835	799764	886160		
RG car production (÷)	372776	388322	369839	433183	371427	450892	389968 (†)	450726 (*)	450666 (ø)	304766 (†)	311705 (†)		
Range Rover	9684	10441	13235	12181	11897	14212	14486	20778	24021	N/A	N/A		
Total UK registrations	1513761	1484713	1555027	1791699	1749647	1832414	1882474	2013693	2215574			1974550	2070852
RG Registrations car (÷)	267357	276989	268124	322665	308965	324574	293240	296784	326432			294171	274332
Range Rover	2521	2394	2696	2991	3089	3381	4226	5027	6175			5415	6254
UK Market share	17.83%	18.82%	17.42%	18.18%	17.84%	17.90%	15.80%	14.99%	15.01%			15.17%	13.55%

(÷) excludes Jaguar / Daimler
(†) includes Rover production of 740 Honda badged vehicles
(*) includes Rover production of 6658 Honda badged vehicles
(ø) includes Rover production of 5044 Honda badged vehicles
(†) includes some Rover produced, Honda badged vehicles

Source SMMT & Motor Industry of Great Britain.

RG PROFITABILITY RECORD

£m

YEAR	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	
PROFIT BEFORE INTEREST AND TAX	117·7	56·7	71·3	-46·2	-293·9	-244·6	-125·8	4·1	-11·7	-49·6	-355·6	27·9	Aggregate -849·7
'BOTTOM LINE' TRANSFER TO/FROM (NEG) RESERVES	44·2	-51·9	-37·7	-144·5	-535·5	-497·0	-292·9	-151·5	73·9 Jaguar Disposal	-163·8	-899·0	-26·9	Negative every year from 1976 except 1984 (Jaguar disposal) Aggregate -2·7 bn

CORPORATE PLAN FORECAST

	FIGS	IN SUPP	MEM		
YEAR	1988	1989	1990	1991	1992
PBIT FORECAST	37·5	52·4	103·8	90·8	142·5 (Turnover 4·26n)
OUTTURN	65·7	41 in H1			

MEMO (COMMERCIAL IN CONFIDENCE)
FIGURES NOT KNOWN TO PAC

AGGREGATE CASHFLOW OUT	-615·1	After total interest of 528·1 – Plan assumed no cash injection
AGGREGATE CASHFLOW EXCL ALL INTEREST BURDEN	-87	

If raised

NO DEPARTMENTAL ACCESS TO RG CURRENT FORECASTS

PROFIT IMPROVEMENT REVIEW FIGURES WERE UNOFFICIAL 'WHAT IF' SCENARIOS NOT FORMAL FORECAST.

OTHER EXPRESSIONS OF INTEREST IN RG IN EXCLUSIVITY PERIOD

By whom?	Interest prior to exclusivity period?	All of RG?	Request for information?
Ford	Had not made an approach since 1986	AR	-
VW	✓ 1987 Discussions with RG	✓	-
Lonrho	1986 interest in LR	✓	✓
Melton Medes	✓ 1987 Referred to RG	✓	✓

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Rover Group plc

4.24 pm

The Secretary of State for Trade and Industry (Mr. Nicholas Ridley): The report of the Comptroller and Auditor General into the sale of Rover Group to British Aerospace is to be the subject of a hearing by the Public Accounts Committee on 4 December. It would not therefore be normal practice for a statement on the subject to be made in the House in advance of that hearing. However, in the light of today's regrettable disclosure of a confidential memorandum submitted to the Committee, I feel under no such constraint.

The report focuses on three broad aspects of the sale. The first is the exclusivity of negotiation granted to BAe. I need not remind the House of the public controversy and uncertainty created by the 1986 discussions with the Ford motor company about its interest in acquiring Austin Rover. It had a serious, detrimental effect on the business, and the Rover board and the Government were determined that the handling of any future privatisation talks should take full account of that experience. Both were convinced that a public auction for the company would be commercially very damaging, and for that reason, following the approach by BAe, it was decided to grant exclusivity for a limited period to see whether a satisfactory agreement could be reached.

Secondly, the report questions the adequacy of the £150 million consideration eventually agreed. I should remind hon. Members of the historical background of Rover Group prior to privatisation. It had already cost the taxpayer £2·9 billion of public funds; that money had been swallowed up in repeated losses while in public ownership. Moreover, the company was dependent on the assurances given by successive Governments in respect of its obligations to banks and trade creditors. That contingent liability on the taxpayer stood at £1·6 billion in March 1988 and was projected to rise over the corporate plan period, because the group's heavy capital expenditure programme outstripped cash generated by forecast trading profits.

Thirdly, the report examines the way in which the negotiations with BAe should have been conducted. Conventional techniques of valuation were clearly inappropriate; it was necessary to approach this as the sale of a going concern, and to strike a reasonable balance between the risks and opportunities confronting BAe as the potential new owners. In that context, I believe that the terms that were eventually agreed represented the best that could be achieved.

Having dealt with the main issues in the NAO's published report, I shall now turn to the confidential memorandum. It is necessary here to recall the fundamental terms of the deal, and the process of their approval. For the business to be privatised successfully, the inheritance of its dismal trading record under public ownership had to be eliminated. In accordance with the state-aid procedures of the European Community, that necessitated exhaustive negotiations with the Commission of an appropriate package.

In July 1988, the Commission agreed a cash injection comprising £469 million in recognition of RG's historic debt, and £78 million in support of its future investment programme in the assisted areas. The Commission was prepared to sanction that aid because Rover Group would henceforth be exposed to the full financial discipline of the market, and because its plans envisaged the elimination of surplus capacity.

When my noble Friend Lord Young disclosed those terms to British Aerospace, the company made it clear that a deal could not be struck on that basis. Four further items were therefore agreed with BAe. First, as BAe wanted to acquire 100 per cent. of the company, the Government agreed a grant of up to £9·5 million towards BAe's costs in buying out the small private shareholding. BAes subsequently bought out those shareholders on terms agreed by itself, Rover Group and their respective advisers to be fair and reasonable.

The second item was a payment of £1·5 million for Rover's privatisation costs. As it was, in effect, Her Majesty's Government who were causing RG to incur those costs, it was only right that Her Majesty's Government should pay them. The third was the waiver of an earlier £5 million contribution that BAe had volunteered towards the Columbus Polar platform programme. In the event, that programme is now undergoing thorough revision, so the whole issue of an industrial contribution is being re-examined.

Finally, the Government agreed with BAe that the precise timing of the payment of the £150 million consideration would follow the clarification of certain tax matters. This delay was time-limited to 31 March 1990.

Those items were addressed where relevant in estimates and reports to Parliament. The Government fully recognised that these additional arrangements were material to the Public Accounts Committee investigation, and from the outset full details were volunteered to the National Audit Office.

The Government took the view that these concessions were essentially separate matters consistent with the terms of the Commission's approval. If the EC Commission now wishes to examine them, the Government will be happy to co-operate.

I believe that these arrangements were the least that were necessary to secure the successful transfer of the Rover Group to the private sector, which was essential fotr the future welfare of the Rover Group and those who work in it, as well as being the best deal available for the taxpayer.

Mr. Gordon Brown (Dunfermline, East): Why were we not told until now about the additional subsidies of £38 million that were given to British Aerospace? Why did the Secretary of State have to be dragged to the House to make those admissions? How does he justify concealing the subsidies on the ground of commercial confidence when the commercial arrangement was not between British Aerospace and a private company but between British Aerospace and the British taxpayer? As it was £38 million of our money, did we not have a right to know?

As for the additional concealed subsidies, will the Secretary of State now confirm that they include offering to buy up to £9 million worth of shares in Rover only to give them back to British Aerospace for nothing; £5 million for British Aerospace's subscription to the European Space Agency which has nothing to do with the Rover Group; potentially £250 million as a reduction in the compensation payable if Rover were sold on in five years and even deferring the final date for payment for up to 18 months, knowing that a deferred price is a lower price?

Regional Transport. In addition, the Jubilee line is to be extended at a cost of about £1 billion, which will bring additional benefits to those using the Underground.

Mr. Alun Michael (Cardiff, South and Penarth): Will the Leader of the House explain in his own words why the matter of the Health Service in Wales has been subsumed in the main body of the National Health Serice and Community Care Bill? Are the Government trying to bury it, especially in the light of the admission by the Secretary of State for Wales that special considerations must be taken into account in respect of the Welsh Health Service?

Will the right hon. and learned Gentleman consider the terms of early-day motion 95?

[That this House notes the considerable time that has elapsed since the Barlow Clowes collapse brought misery and worry for thousands of people, many of whom were elderly individuals who had placed their money in what they believed to be a safe Government-approved investment, and who were shocked to discover its true nature; hopes that early publication of the Ombudsman's report will clearly illuminate the events leading up to the collapse; but notes that apportionment of blame and eventual repayment will come too late for people who should have been able to enjoy security and freedom from worry in their twilight years—some of whom, sadly, have already died—unless the Government now belatedly adopts the pro-active role urged by the Opposition by launching a lifeboat scheme and drawing together all those with a legitimate interest in the compensation of investors to achieve an early payout without further delay or unproductive litigation.]

Will he ask the Secretary of State for Trade and Industry to make an early statement on the Barlow Clowes scandal, and may we have a positive, proactive stance by the Government, which would give some hope to the many elderly people who, through no fault of their own, are suffering the effects of that company's collapse long after it was first brought to the attention of this House?

Sir Geoffrey Howe: It is difficult to respond to several substantive points together when dealing with the business of the House. As to the hon. Gentleman's second point, all right hon. and hon. Members share his concern about the implications of the collapse of Barlow Clowes. The draft report of the Parliamentary Commissioner is now being considered and will receive a response as soon as possible. It would not be appropriate for the House to debate that matter until the report has been finalised. However, clearly it is an important matter.

As to the Health Service in Wales, neither I nor anyone else can alter the Principality's constitutional status as it was established by Henry VIII. However, we can be assured that my right hon. Friend the Secretary of State for Wales will continue to take the energetic care that he always does of the Welsh Health Service.

Mr. Richard Holt (Langbaurgh) *rose*——

Mr. Speaker: Order. Was the hon. Member present in the Chamber when next week's business was announced?

Mr. Holt: I have been in my place since 2.30 pm, Mr. Speaker, but I have twice been unsuccessful in trying to catch your eye.

Mr. Speaker: In that case, I call the hon. Member.

Mr. Holt: Will my right hon. and learned Friend reflect on the request made by the hon. Member for Bradford, South (Mr. Cryer) for an education debate so that the House may discuss the Cleveland city technology college, which has been a great success despite the pernicious and vicious attitude of the local education authority, which even seeks to ban other schools from playing soccer against 10-year-olds?

Sir Geoffrey Howe: If the House has another opportunity to debate education, my hon. Friend will be well placed to repeat the important point that he has just made.

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Is not the real reason why the Government asked for details of the sale to be kept confidential not a commercial one, because the Minister has not made a commercial case, but the party political embarrassment that would be caused by the revelation of those subsidies?

In those circumstances, given the additional level of subsidy—£38 million—how could his Department have thought that there was no necessity even to inform the European Commission that those subsidies were paid? How can the Prime Minister tell other countries in good faith that they should abolish hidden subsidies before she joins the exchange rate mechanism when she has allowed exactly those hidden subsidies?

Now that the Comptroller has named four other companies that were interested in the Rover Group, and, according to the lunchtime news, one has said that it put its interest in writing, how can the Secretary of State defend the statement of the former Minister, Lord Young, that

"British Aerospace was the only company to approach me to buy Rover",

especially when we now know that Ministers were advised by their own advisers, Baring Brothers, that they should create a competitive market?

As we now know that most of Rover's debts were written off by the Government, that assets in shares in other companies were known by the Government to be worth more than £100 million, that surplus sites that were thrown in are are now worth more than £33 million and that Rover's forecasts were not for losses but for profits totalling £400 million over the next five years—money that could have gone to the taxpayer—how can the Secretary of State now justify selling Rover for only £150 million?

I want a direct answer to this question: is it right that, so far, little or nothing has yet been paid by British Aerospace despite the fact that British Aerospace has made substantial profits from Rover and has already sold assets worth £126 million? Is the issue not the past investment to make Rover profitable, but what the taxpayer and the public could have gained in future as a result of that public investment?

Finally, in those circumstances, how can the Minister possibly deny the serious charges of mismanagement, incompetence and a serious waste of national resources by the Government? Is it not the case that they were interested in privatising Rover at any price and at any cost rather than securing what is in the national interest? Is it not time for open Government in this matter and is it not the case that our only hope for open Government is a Labour Government?

Mr. Ridley: The items that I mentioned in my statement today were addressed, wherever relevant, in the estimates and reports to Parliament. Full details were made available to the Comptroller and Auditor General when he started his inquiries, as was completely correct. The House is not being told now; the Public Accounts Committee was told before. Nor have I been dragged to the House. I volunteered to make the statement for the convenience of the House. I have made an open statement, so I reject any suggestion that I have sought to conceal anything.

British Aerospace wished to acquire 100 per cent. of the company. We were not in a position to sell it 100 per cent. of the company because there were minority shareholders. It was prefectly right and proper that we should have enabled it to buy out those minority shareholders, because it was much more simple procedurally for it to do so than for the Government to do so directly.

The £5 million for the space project was nothing to do with the motor industry and therefore, in our opinion, nothing to do with the deal reached with the Commission.

The hon. Member for Dunfermline, East (Mr. Brown) seems to be unaware that the reduction in the writing-off of debt, which the Commission insisted be made during negotiations with it, reflected itself in a reduction of what the company would have had to pay back in the event of a sale within five years of the assets and trademarks of the Rover Group. It was right that that figure should have been reduced commensurate with the reduction in the injection of cash made by the Government.

As I have told the House, we had reached agreement with the Commission when these additional items became necessary. The late payment was mentioned in the statement by my right hon. and learned Friend the Member for Rushcliffe (Mr. Clarke), the then Chancellor of the Duchy of Lancaster, on 14 July last year. We took the view that the other items to which I have referred were consistent with the Commission's terms, and that as they did not affect the competitiveness of the Rover Group's production, disclosure was not necessary. Any question of reopening the procedure would have jeopardised the deal.

As to the last point made by the hon. Member for Dunfermline, East, far from being a rip off, let me quote what the hon. Member for Dagenham (Mr. Gould) said when the deal was announced by my right hon. and learned Friend. He said:

"How is it that British Aerospace has now accepted £250 million less than Ministers initially offered?"

The hon. Gentleman continued:

"Is it true that institutional shareholders have already been telephoning to express their objections?"—[*Official Report*, 14 July 1988; Vol. 137, c. 613.]

The allegation then was that we had screwed British Aerospace too hard. Now, the hon. Member for Dunfermline, East is saying that the deal was far too soft. The only conclusion that we can draw from that is that it is easy to be wise after the event and that the hon. Gentleman is suffering from an overdose of hindsight.

I should add that no payment has been recieved. British Aerospace has until the end of March next year.

Mr. Michael Grylls (Surrey, North-West): Will my right hon. Friend accept that it is obvious from the rather synthetic annoyance of the Opposition that they cannot bear the fact that, because of the Government's successful policies, Rover is now a successful company in the private sector? When they were in office, all they did was pour more and more of taxpayers' money into it, and it lost more and more year after year. We have been successful with it.

Is it not true that the financial terms agreed between Rover and British Aerospace were hugely advantageous for the taxpayer, who has been relieved of an enormous contingent liability of £1·8 billion? That must be to the advantage to the taxpayer.

Mr. Ridley: I agree entirely with my hon. Friend. The deal was of great advantage to the taxpayer in staunching the losses that the Rover Group had incurred. The deal was struck in July 1988, but the only deal that could have been done was one agreed by the buyer and seller. In this case, the buyer had grave doubts about whether it wished

[Mr. Ridley]

to proceed, and it almost aborted the sale at the last minute. It did not show any signs whatever that it was not taking great risks in taking on the Rover Group.

Mr. Peter Snape (West Bromwich, East): Is there no limit to the Secretary of State's arrogance on these matters? Is he aware that the only reason why he is at the Dispatch Box is to pre-empt the inevitable row that would follow this morning's publication of the memorandum in *The Guardian*? His whole approach typifies the Government's unethical approach to the disposal of public assets. A more fitting place for his talents would be in a used car lot where, as the usual sweetener he would throw in the whole car factory.

Mr. Ridley: The hon. Gentleman's style is not appropriate on this occasion. It was correct for the Public Accounts Committee to consider the memorandum confidentially. If the memorandum had not been leaked, the Committee could have considered the matter and concluded whether publication was in the national interest. That would have been far the better way to handle the matter. I regret that the PAC has been pre-empted because that has made the matter more difficult to handle. However, as soon as it happened I took the correct action of coming to the House to make a statement.

Mr. Kenneth Warren (Hastings and Rye): Does my right hon. Friend accept that the openness of his declaration is welcome? Will he further accept that as chairman of the Select Committee on Trade and Industry, which last year conducted extensive inquiries into the purchase of Rover by British Aerospace, I would have found it helpful if the memorandum had been submitted to the Committee in confidence. With regret, I find unacceptable his statement that the conventional valuations were not appropriate. When my right hon. and noble Friend was asked by the Select Committee whether he had put a valuation on the machinery and assets of Rover, it was to our surpprise that he replied no. The negotiations could have been handled by the Department much more professionally and I hope that in future that will be the case.

Mr. Ridley: The Committee may wish to follow up the question of what memorandum was put before it but I was not aware of the point that my hon. Friend raised. The sale was not and could not have been normal. The House will remember when the possibility arose that Rover would be sold to the Ford Motor Company. As a result, there was virtually a public auction. We debated the matter many times in the House but it was possible to resolve it because of the political temperature. Rover informed everyone involved that the position was extremely damaging to its business and at the time it lost market share. My right hon. and noble Friend had no alternative but to conduct exclusive negotiations with an acceptable British company and only one had expressed interest at that time. [HON. MEMBERS: "Not true."] After it had been announced that the deal would be negotiated exclusively, other companies expressed interest. It would have been wrong for my right hon. and noble Friend to go back on the undertaking that the negotiations would be exclusive.

Mr. Terry Davis (Birmingham, Hodge Hill): If the financial arrangements were as straightforward as the Secretary of State suggests and were already available in the estimates presented to the House, why did his Department ask the National Audit Office to leave them out of the report published two days ago?

Mr. Ridley: As I said, we did not wish to draw attention to the arrangements in the July statement because it was important that the Commission should not re-open the whole matter. The matters that I reported were not relevant to the agreement that we made with the Commission. In view of the sensitivity of those facts, I thought it right that the PAC should decide for itself whether it was in the national interest to publish them. I regret that the PAC's right to decide has been pre-empted.

Sir Hal Miller (Bromsgrove): Does my right hon. Friend recollect that about a month ago he was criticised for not keeping Jaguar British? Today he is criticised for keeping Rover British and for its success. Does he agree that the Opposition have no interest in the success of any British industrial company? Did we hear any request for a statement yesterday about the additional investment in the British motor industry? Will he reconsider his description of the Opposition as being wise after the event? It is clear that they are unable to appreciate the difficulty of valuing what was a bankrupt company trading insolvently under Government guarantees?

Mr. Ridley: The transformation in the health of the Rover group after many years of decline and massive losses is justification for its sale to the private sector, if ever one were wanted. I agree that the Opposition are now to be described as unwise after the event.

Mr. Dave Nellist (Coventry, South-East): Is the Secretary of State aware that tonight in Coventry many thousands of Rover workers will wonder whether we are witnessing the Government's incompetence or their corruption? Is it not clear that, with £600 million of cancelled debt, £60 million of underselling and the £38 million of back-handers revealed today, the privatisation of Rover was legalised theft? Is he aware that British Aerospace knew in advance of the land values, the value of subsidiary companies such as the Spanish company and Daf and of stocks and shares and is laughing all the way to the bank? The right hon. Member for Chingford (Mr. Tebbit) stayed in the Chamber long enough to make sure that the Prime Minister held her line at Question Time. Why is he not here now to make a statement about his previous role as Secretary of State for Trade and Industry from which he went directly to be chief adviser to the board of directors of British Aerospace? More than any other privatisation deal, this deal stinks to high heaven.

Mr. Ridley: Thousands of Rover workers wandering about Coventry will be grateful that their company is beginning to move ahead, investment is being put into it and the days of its failures and loss-making under public ownership have come to an end. The fulfilment of that goal makes worthwhile the deal that was done to achieve it. For the hon. Gentleman's benefit, to my knowledge no Land Rover assets have been sold.

Mr. Steve Norris (Epping Forest): Does my right hon. Friend agree that with hindsight we are all millionaires? Does he further agree that any business man who was prepared to pay asset value for a company haemorrhaging hundreds of millions of pounds without the slightest

realistic prospect of ceasing to do so would be considered insane? Is he aware that those of us who were anxious that the deal should go through were disturbed that at the last minute the board of British Aerospace was so unsure whether the sale should proceed that it delayed the final announcements to be made by the then Secretary of State? Is it not true that when the details of the events are examined it will be clear that according to commercial logic the Government did an exemplary deal in selling Rover to British Aerospace?

Mr. Ridley: I wish to disagree with my hon. Friend in one respect: many hon. Gentlemen, even with the advantage of hindsight, would succeed in losing millions. [HON. MEMBERS: "What did the right hon. Gentleman do?"]

Mr. Speaker: Order.

Mr. Ridley: My hon. Friend's other point, that British Aerospace hesitated on the eve of signing the deal, is absolutely true. I can confirm that it nearly decided to abort the takeover because it did not feel that it could live with the risks. It decided to go ahead, which is infinitely to the benefit of the workers and customers of the Rover Group.

Mr. Andrew Smith (Oxford, East): Is it not the case that the Secretary of State cannot begin to understand the anger and anxiety of Cowley workers and their families during the whole period of the shameful conduct of the sale? Is it not evident that Conservative party political determination to sell Rover at any price and in any way has counted for everything and that the interests of the country, taxpayers and the work force has counted for nothing? Is it not essential that in addition to seeing proper accountability to the taxpayer for taxpayers' money, any surplus arising to British Aerospace in this sorry affair should be invested in production and jobs at Cowley, not asset stripped?

Mr. Ridley: The deal has been done and cannot be re-opened. I understand that British Aerospace intends to make massive investments in the Rover Group—more than £1 billion—to develop its capacity and model range for the future. That is precisely what the hon. Gentleman asks for.

Mr. Roger King (Birmingham, Northfield): Is my right hon. Friend aware that the people of the west midlands will contrast this Government's support for the British motor industry and the glittering future that Rover Group now has in the private ownership of BAe with the glittering, wonderful future that the Labour Government gave the Meriden motor cycle co-operative?

Mr. Ridley: Yes. Because of the many changes that have taken place under this Government the British motor industry is beginning to move ahead and to increase its market share in Britain and throughout the world. We shall see a large increase in motor car production in the years ahead.

Mr. Doug Hoyle (Warrington, North): Does the Secretary of State realise that only one Conservative Member, the hon. Member for Hastings and Rye (Mr. Warren), seems concerned about taxpayers having a fair deal? [HON. MEMBERS: "We are all concerned about that."] Will the Secretary of State please answer his hon. Friend's questions? Why was the memorandum not put before the Select Committee on Trade and Industry? Is he aware that it is inadequate to answer that the Committee can now inquire into the matter? Does he agree that the memorandum should have been made available at the time? Was the Commission aware that if Rover were re-sold in the following five years, the group would not have to repay the £650 million, but only £400 million? In view of the disclosures, will the Secretary of State tell BAe that it cannot have until March before paying the £150 million, but must pay without delay because it has benefited from the swindle?

Mr. Ridley: If hon. Gentlemen have taxpayers' interests at heart, they should recognise that the £3·5 billion which was expended on the Rover Group while it was in the public sector was the biggest drain that could ever been placed on taxpayers' shoulders and that from now on the Rover Group is beginning to pay tax which is to the taxpayers' benefit. My right hon. and noble Friend who handled the matter appeared before the Select Committee on Trade and Industry, and he must be allowed to give the evidence and produce the papers that he thought appropriate at the time. The hon. Gentleman is not right when he says that that £450 million will have to be repaid. The £650 million was the sum before the Commission reduced the amount which the British Government could give to assuage Rover's debts. As the Commission reduced the sum, it was right that the amount to be repaid should also be reduced.

Sir Giles Shaw (Pudsey): Does my right hon. Friend agree, as one who had a part to play in the developments at Rover at a certain time, that the problem with the company, apart from wholly inherited debt and the fact that it was trading insolvently in all but name, was the fact that the Varley-Marshall agreement entered into by the Labour Government provided never-ending commitment to the Government of the day to stand behind every bill that the company happened to offer? Will he further consider that while enormous efforts were made to maintain productive investment, this incredibly bankrupt company would have been closed long ago had it not been for the arrangements with BAe? Does my right hon. Friend agree that that was the real alternative offered?

Mr. Ridley: My hon. Friend is absolutely right. He talks of what came to be known as the Varley-Marshall-Joseph undertakings and they totalled £1·6 billion by March last year. I am extremely glad that they will never be known as the Varley-Marshall-Joseph-Ridley undertakings.

Mr. Simon Hughes (Southwark and Bermondsey): Can the Secretary of State answer the questions that he has still not answered? How does he reconcile the uncorrected public announcement that if BAe sold Rover within five years the payback would be £650 million, when it would be £400 million? How does he reconcile the Prime Minister's statement about the valuation in a letter to my right hon. Friend the Member for Yeovil (Mr. Ashdown) on 21 November 1988 that

"the value to be attached to assets . . . is at present purely speculative",

with his statement this afternoon that the price was reached by striking a reasonable balance between risks and objectives? How does he reconcile his declaration that he is in favour of no support, a strong competition policy

[Mr. Simon Hughes]

within the EC and upholding the law, with his subsidisation without telling the EC, thereby breaking the law and his own declared policy?

Mr. Ridley: The hon. Gentleman is wrong. The adjustment to the ceiling of any penalty for a sale within five years was indeed communicated to the Commission. It was twice reduced because the Commission reduced the original consideration. The conclusion of a valuation between a seller and a buyer must be the price at which the buyer is prepared to buy and the seller to sell. That is the price that was finally agreed last July.

Mr. Simon Coombs (Swindon): Is my right hon. Friend aware that while Austin Rover was in the public sector the plant at Stratton near Swindon was a frequently mentioned candidate for closure and that since Rover has been in the private sector that plant has been the recipient of £17 million of new investment from BAe? Does my right hon. Friend draw any conclusion from that? Can he tell the Opposition how many new hospitals and schools could have been built with the money that for many years haemorrhaged into Austin Rover while it was in the public sector? Can he tell us what efforts he is making to find the person who leaked the document?

Mr. Ridley: On the latter point, it is not for me but for the PAC to re-establish its reputation for looking after the financial and confidentially financial interests of this House. I am glad to hear that the privatisation of the Rover Group has led to increased investment in my hon. Friend's constituency. It will lead to increased investment in many other constituencies as the momentum increases.

Mr. Geoffrey Robinson (Coventry, North-West): In the light of the Secretary of State's answers this afternoon the only thing for which the House can be grateful is that it was not he who negotiated the deal. If he had, it would have been an even bigger rip-off than it was. *[Interruption.]* We have yet to receive a successful answer to two shocking revelations, first, that not one penny has yet been paid by BAe and, secondly, that the British Government surreptitiously paid £38 million. *[Interruption.]* Finally—*[Interruption.]*

Mr. Speaker: Order. The hon. Gentleman must have a chance to put his questions.

Mr. Geoffrey Robinson: Is the right hon. Gentleman aware that in the light of those revelations and the inadequacy of his answers about them, the Government have forfeited any remaining claim that they ever had to be from the party of financial responsibility and managerial competence?

Mr. Ridley: It is a rare and well deserved tribute to my noble Friend Lord Young that the hon. Gentleman believes that he negotiated an even better deal than I would have done. I am grateful to the hon. Gentleman. I have dealt with the rest of his question because I gave full, open and satisfactory answers to all the points that were raised.

Several Hon. Members *rose*——

Mr. Speaker: Order. I remind the House that there is another statement today and a debate on a Public Accounts Committee report. I understand that the Public Accounts Committee is to discuss this matter tomorrow and no doubt we shall return to it later. I will allow three more questions from each side and then we must move on.

Mrs. Maureen Hicks (Wolverhampton, North-East): As a west midlands Member and the proud owner of a British Rover car, I feel duty bound to pay tribute to the success of Rover in private hands. Thanks to the vision of the Government, Rover has gone from strength to strength and has secured the jobs of many midlands workers. Will my right hon. Friend confirm that the Government dealt exclusively with British Aerospace because of pressure from the House not to sell to an overseas company?

Mr. Ridley: My hon. Friend is quite right. I remember, although at the time I was not in the Department, the extraordinary political clamour surrounding the possibility of selling the company to Ford. Therefore my noble Friend had no alternative, when he finally got a serious offer from British Aerospace, but to undertake to negotiate exclusively lest a situation such as that which had developed previously arose again.

Mr. D. N. Campbell-Savours (Workington): Is it not clear that the noble Lord Young must have set out deliberately to mislead the European Commission by failing to indicate——

Mr. Speaker: Order. That is a reflection on a Member of the Upper House. The hon. Gentleman must withdraw that comment.

Mr. Campbell-Savours: If I have used a word that you wish me to withdraw then I do so.

The Department misled the European Commission by failing to tell it that concessions were being made and that subsidies were being paid. What credibility do we now have with people in the European Community who have been complaining about the stiff position of the Government on the whole question of regional subsidies and sectoral support?

Mr. Ridley: That is not the case. My noble Friend considered that the agreements that he had made beyond the main deal in relation to the sale of the Rover Group did not come within the competence of the Commission in relation to state aid. I have explained why I think that that was right. If the Commission does not agree it can comment in the future. We wait to see what it says.

Mr. James Cran (Beverley): Does my right hon. Friend agree that in evidence to the Select Committee on Trade and Industry the chairman of Rover, speaking on behalf of his whole board, gave absolute backing to the Government on their action? The board gave as the precise reason for that the fact that it did not want a public auction and the consequential adverse effects that that would have on the dealer network, the work force and the customer.

Mr. Ridley: So far I have not heard any hon. Member question the fact that it was correct to engage in exclusive negotiations, and that is because of the reason that my hon. Friend has given. If that be so, no one could question the deal that was finally agreed with British Aerospace, especially as it was regarded at the time as extremely risky and unfair to British Aerospace to undertake such large risks for the consideration that they offered.

Mr. Brian Sedgemore (Hackney, South and Shoreditch): Can the Secretary of State tell us whether his permanent secretary as accounting officer for the Department has put in an accounting officer's minute complaining about what went on? Is the right hon. Gentleman aware that if the directors of a public company acted in the way in which he has acted, the fraud squad would long since have had them in the dock at the Old Bailey for corruptly defrauding their shareholders?

Mr. Ridley: My permanent secretary as accounting officer has made a complete disclosure to the Comptroller and Auditor General on all these matters. That is the confidential memorandum that the Public Accounts Committee is receiving. He has made not comment other than to make sure, as I have said, that the PAC was aware of all these matters.

Mr. Neil Hamilton (Tatton): Does my right hon. Friend agree that it is rather quaint to hear Opposition Members complaining about an illusory loss of £38 million when we did not hear a peep from them about the loss of 100 times that amount—£3·5 billion—which can be laid at Rover's door over recent years? We wholly endorse the Government's position on the sale. The difference between my right hon. Friend and the Opposition is like the difference between a Rover Sterling and a Trabant.

Mr. Ridley: I entirely agree with my hon. Friend whose comments are borne out by what I have said. I enjoyed his description of the Opposition as a Trabant.

Mr. Eric S. Heffer (Liverpool, Walton): Those of us who were in the Department of Trade and Industry when British Leyland and Rover were partners, remember that the company had to be taken into public ownership because it was on the point of collapse. The Government of the day had no choice because they had to save the jobs of the people in the industry. If we had not taken the company into public ownership there would have been mass unemployment. Perhaps the right hon. Gentleman would have liked to see those workers being put out of work. Obviously, Conservative Members have a short memory about what actually happened. Because of the attitude of the right hon. Gentleman and the Government, money has been lost, although I am not saying that they had their fingers in the till. If they were councillors they would have been disqualified and surcharged. It is high time that the right hon. Gentleman resigned.

Mr. Ridley: If I were the hon. Member for Liverpool, Walton (Mr. Heffer) I would sit this one out and not admit to having played such a prominent role in the waste of the £3·5 billion to which I have referred.

Straw and Stubble Burning

5.7 pm

The Minister of Agriculture, Fisheries and Food (Mr. John Gummer): With permission, Mr. Speaker, I should like to make a statement.

Hon. Members will be well aware of the considerable problems this year on straw and stubble burning, and will recall a similar situation in 1983 when there were many complaints from the public. *[Interruption.]*

Mr. Speaker: Order. Hon. Members who do not wish to remain for the statement should leave quietly.

Mr. Gummer: In 1984 the Royal Commission on environmental pollution recommended a ban on straw burning to come into force within five years. By then, the Government had already drawn up model byelaws providing for greatly enhanced controls, and the National Farmers Union had issued a toughened code of practice in 1986. A ban on burning was therefore not judged to be necessary.

However, in 1989 the problems have returned with a vengeance. There have been many cases of smoke drifting across roads, in some cases with disastrous results, smoke-filled homes, dirty smuts, and genuine fears for the safety of property. In addition, there have been considerable losses of hedges and trees and, of course, wildlife. I have received more than 600 letters, many of which have been from hon. Members in all parts of the House and my Department has received notification of more than 2,500 complaints.

I have, therefore, ordered a thorough review of the policy and the effectiveness of existing controls. I have considered the alternatives carefully so that I can respond first to the public's concern, secondly to farmers' concerns that prohibiting straw burning completely will add to their costs, and thirdly to the fact that the reputation of the farming community suffers inevitably from the consequences of this practice on others who live in the countryside.

I note that the NFU has not come out in favour of a ban, but has instead proposed a licensing scheme, charging for the issue of licences and withholding them from farmers with a poor track record. There are, of course, legal difficulties with the scheme, in terms of withholding of licences on a discretionary basis, but in my view the strongest argument against the licensing proposal is that it would be unlikely to result in any significant reduction in burning.

The Government have therefore decided that straw and stubble burning should be banned. If Parliament agrees to the ban, it will come into force in England and Wales in the late autumn of 1992. That will give farmers three seasons to adjust to the new situation and to develop alternative methods of cultivation. That seems to be a proper balance between the demands of people who live in the countryside and the consideration that we would give to any section of the community to enable them to meet the needs of the whole community.

Accordingly, during the passage of the Bill which will be introduced to give new powers to control pollution and waste, the Government will be seeking the necessary powers to ban straw and stubble burning. The powers will also enable me to grant exemptions, but I should like to make it clear that although I intend to consult the industry on their scope, any exemptions will be limited—for

[Mr. Gummer]

example, to a specific crop such as linseed. I do not propose to introduce a system of licences for farmers permitted to burn under those exemptions.

I shall also discuss with the NFU how the existing code of practice should be strengthened and applied during the period leading up to the proposed ban.

Mr. David Clark (South Shields): I congratulate the Minister on his decision to ban the anti-social and anti-environmental practice of straw burning. This year straw burning has become an unacceptable public nuisance in many parts of Britain. The NFU code of practice and local authority byelaws plainly have not worked, and the Minister is right to announce his intentions today. It has long been the policy of the Labour party to ban straw burning. We therefore support the Minister and welcome his conversion.

The Minister referred in his statement to seeking powers in the course of the anti-pollution Bill. Will he give the House an assurance that there will be a representative of his Ministry on the Committee of that Bill to ensure that that aspect of agriculture and land use will be fully aired because it is an important matter and there are difficulties involved?

As the Minister knows, it is not enough simply to ban straw burning. We need to turn our attention to the problem of what to do with the surplus straw. Obviously, there are occasions when straw can be incorporated and it can be fed to animals, but there are times when those means are not appropriate. With a little ingenuity and innovation, surplus straw can be used to positive environmental effect.

Have the Government any plans to encourage that? Will the Government be providing financial assistance for research and development into other uses of straw? For example, it could be used in the construction industry, as a timber substitute—in contiboard and plywood panels. Are the Government prepared to assist companies such as British Sugar which, I understand, is contemplating a straw-powered paper-making plant in east Anglia? It is vital that those aspects of straw burning should be seriously considered. Otherwise the sound environmental benefits of banning straw burning may be lost.

Mr. Gummer: I thank the hon. Gentleman for his support. I assure him that the Parliamentary Secretary my hon. Friend the Member for Skipton and Ripon (Mr. Curry), who has responsibility for farming, will sit on the Committee of the Bill to represent the interests that the hon. Gentleman mentioned and to ensure that the proposal is carried to fruition.

The Government are already spending some £700,000 on the research to which the hon. Gentleman referred. I am interested in the use of straw to make boards. Stramit is a major organisation in Suffolk which has done a great deal of work to develop that, and I pay tribute to the important exports of machinery developed by that company.

There is a plan by British Sugar to develop a large factory, not using straw as a fuel but using it in the paper industry. That has a real chance of success, and I have no doubt that various plans will be announced as they come to fruition. I am sure that they will receive the support that they deserve.

Several Hon. Members *rose*——

Mr. Speaker: Order. I remind the House that there is an important debate after this on the Public Accounts Committee report. I know that this subject is of great interest to right hon. and hon. Members but the proposal will come into effect in 1992 and there is to be a Bill, so there will be other opportunities to dicuss the matter. I should like to get on to the debate on the PAC report at 5.30 pm, so I hope that hon. Members will keep their questions brief.

Sir Hector Monro (Dumfries): Although my right hon. Friend is right about what he is doing for the environment, has he given sufficient thought to the problems of farmers, bearing in mind that their incomes are substantially lower than they were some years ago, and how they can find ways to dispose of the straw within three years? From a husbandry point of view, it is difficult to find an alternative.

Will the Minister also give an assurance that Muirburn in the hills will not be affected because it is an essential part of the regeneration of grass and heather in the uplands?

Mr. Gummer: I can certainly give that assurance to my hon. Friend and I shall consider the effect of the ban on the farming industry. However, if we do not have such a ban, the price paid by farmers every year in terms of the effect upon public confidence and attitudes will be higher than any loss that may arise from the ban. Many farmers who used to think that straw burning was essential have already found alternatives. I believe that the industry will find ways of complying with the ban in the three years to come. I suspect that if the ban had not been announced now alternatives would be unlikely to be found within three years.

Mr. Geraint Howells (Ceredigion and Pembroke, North): I am delighted that the Minister has accepted the views of my colleagues on the Liberal benches and those of many right hon. and hon. Members on both sides of the House. I congratulate him because on this occasion he has made the right decision. It is long overdue, but all hon. Members should co-operate and work with the Minister.

The Minister has given farmers two or three years to put their house in order. We have learnt from the mistakes of 1983-84 when milk quotas were delivered overnight. We should all back the Minister and the Government during the proceedings on the Bill.

Mr. Gummer: I thank the hon. Gentleman for his support. There is always a likelihood that a policy will be successful when it has many parents.

Mr. Jerry Wiggins (Weston-super-Mare): Is my right hon. Friend aware that the planned British Sugar plant will consume some 750,000 tonnes of straw per year—10 per cent. of annual production—but that the innovative nature of the technology required and the high risks involved mean that it may need substantial contributions from the Government? Will the Minister make representation to the Department of Trade and Industry in favour of that excellent British enterprise?

Mr. Gummer: We are not at that stage yet, but the proposals, albeit in their early stages, certainly look attractive. There is also the European dimension, which I shall consider with care and thought.

With the Compliments of

Rt. Hon. Sir Edward du Cann, KBE

LONRHO Plc

Cheapside House,
London EC2V 6BL.

Tel: 01-606 9898

Note

Agreed with DTI no need for any No. 10 acknowledgement.

RRC6 30/11.

LONRHO

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From: The Chairman,
The Rt. Hon. Sir Edward du Cann, KBE

30th November, 1989

Dear Mr Bower.

As you know, I was Chairman of the Public Accounts Committee between 1974 and 1979 and the first Chairman of the newly established Public Accounts Commission during the last Parliament. I therefore follow the affairs of the Comptroller and Auditor General's department and the Public Accounts Committee with more than usual interest and sympathy.

I have been particularly concerned to read the report of your department into the sale of the Rover Group. There is one aspect of this matter which I think should be drawn to your attention and to the attention of the Public Accounts Committee, of which I have particular knowledge and of which you may have been unaware when you wrote your report.

Chapter 3, paragraph 5 of the report clearly states that no firm offers were received for Rover other than the bid from British Aerospace. The implication is equally clear, and it was reinforced in the subsequent Parliamentary exchanges between the Prime Minister and the Leader of the Opposition, namely that because there were no bids from any of the other companies which had expressed interest in Rover the Department of Trade & Industry had no alternative but to sell the business to British Aerospace. Any inference of this kind would be wholly wrong.

Lonrho Plc was seriously interested in making a bid for Rover. We made our intentions entirely clear to the Department of Trade & Industry in correspondence at the time. We had earlier, i.e. before the exclusive arrangements made by the Department of Trade and Industry with British Aerospace - expressed interest in Land Rover. Requests were made for information to be given to us on the basis of which a firm bid could be tendered. This information was consistently refused. It was because we did not have the information on which to base our bid that a bid was not made. Had that information been supplied to us it is certain that a competitive a bid would have been made. I expect that other potential bidders were in the same position. We were all excluded from bidding.

At the time we considered that the way in which the matter was handled by Government was extraordinary. We stated our belief that the best price for Rover would be obtained through open negotiations and asked that the exclusivity granted to British Aerospace be reconsidered. We see no reason to change our opinion now.

Registered office as above
Registered in England No. 103002

Statements to the effect that British Aerospace alone were interested in acquiring Rover are untrue.

If there is any further information I can give you please do not hesitate to ask.

As a matter of courtesy I am copying this letter to the Chairman of the Public Accounts Committee, the Rt. Hon. Robert Sheldon, MP, the present Secretary of State for Trade & Industry, the private secretary to the Prime Minister and the private secretary to the Leader of the Opposition.

Yours sincerely,

Edward du Cann

John Bourn, Esq., CB,
Comptroller & Auditor General,
National Audit Office,
157-197 Buckingham Palace Road,
London SW1W 9SP

PRIME MINISTER

The Rover Statement went as well as could be expected. It was a fairly sparsely attended House. Gordon Brown did not press his attack with great skill: he concentrated on whether the £38 million additional payment represented a poor deal for the taxpayer, rather than on whether the House or Commission had been fully informed. Kenneth Warren was the only unhelpful Government backbencher: he expressed criticism both that the Trade and Industry Select Committee, which had looked into the Rover sale earlier this year, had not vouchsafed the confidential memorandum, and asserted that the valuation had not been handled professionally by DTI. By contrast, Hal Miller and Steve Norris, who both have Rover plants in their constituencies, were very helpful and supportive of Nick Ridley. The best question from the Opposition, which Nick Ridley ducked, was why if all the necessary information was available in the estimates, had DTI felt it necessary to ask the PAC to keep the memorandum with these details confidential.

My assessment, which DTI share, is that the heat has gone out of this issue, at least until Monday when Sir Peter Gregson makes his appearance before the PAC.

DOMINIC MORRIS
30 November 1989

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SALE OF ROVER GROUP PLC
THURSDAY 30 NOVEMBER 1989
STATEMENT BY SECRETARY OF STATE FOR TRADE AND INDUSTRY
THE RT HON NICHOLAS RIDLEY MP

1 The report of the Comptroller and Auditor General into the sale of Rover Group to British Aerospace is to be the subject of a hearing by the Public Accounts Committee on 4 December. It would not therefore be normal practice for a Statement on that subject to be made in the House in advance of that hearing. However, in the light of today's regrettable disclosure of a confidential memorandum submitted to the Committee, I feel under no such constraint.

2 The report focuses on three broad aspects of the sale. First the exclusivity of negotiation granted to BAe. I need not remind the House of the public controversy and uncertainty created by the 1986 discussions with the Ford Motor Company about their interest in acquiring Austin Rover. This had a serious, detrimental effect on the business and the Rover Board and the Government were determined that the handling of any future privatisation talks should take full account of that

experience. Both were convinced that a public auction for the company would be commercially very damaging and for this reason, following the approach by BAe, it was decided to grant exclusivity for a limited period to see whether a satisfactory agreement could be reached.

3 Second, the report questions the adequacy of the £150m consideration eventually agreed. I should remind Hon Members of the historical background of Rover Group prior to privatisation. It had already cost the taxpayer £2.9bn of public funds; this money had been swallowed up in repeated losses while in public ownership. Moreover the company was dependent on the Assurances given by successive Governments in respect of its obligations to banks and trade creditors. That contingent liability on the taxpayer stood at 1.6bn in March 1988 and was projected to rise over the Plan period, because the Group's heavy capital expenditure programme outstripped cash generated by forecast trading profits.

4 Third the report examines the way in which the negotiations with BAe should be conducted. Conventional techniques of valuation were clearly inappropriate. It was necessary to approach it as the

sale of a going concern and strike a reasonable balance between the risks and opportunities confronting BAe as the potential new owners. In this context I believe that the terms eventually agreed represented the best that could be achieved.

5 Having dealt with the main issues in the NAO's published report, I shall now turn to the confidential memorandum. It is here necessary to recall the fundamental terms of the deal and the process of their approval. In order successfully to privatise this business, the inheritance of its dismal trading record under public ownership had to be eliminated. In accordance with the State Aid procedures of the European Community this necessitated exhaustive negotiations with the Commission of an appropriate package. In July 1988 the Commission agreed a cash injection comprising £469m in recognition of RG's historic debt and £78m in support of its future investment programme in the Assisted Areas. The Commission was prepared to sanction this aid because Rover Group would henceforth be exposed to the full financial discipline of the market and because its plans envisaged the elimination of surplus capacity.

6 When my Noble Friend disclosed these terms to British Aerospace the company made it clear that a deal could not be struck on this basis.

7 Four further items were therefore agreed with BAe:

(i) BAe wanted to acquire 100% of the company. The Government therefore agreed a grant of up to £9.5m towards BAe's costs in buying out the small private shareholding. BAe subsequently bought out those shareholders on terms agreed by itself, Rover Group, and their respective advisers to be fair and reasonable.

(ii) A payment of £1.5m for Rover's privatisation costs. Since it was in effect HMG which was causing RG to incur those costs, it was only right that HMG should pay them.

(iii) Waiver of an earlier £5m contribution BAe had volunteered towards the Columbus Polar platform programme. In the event that programme is now undergoing thorough revision so the whole issue of an industrial contribution is being re-examined.

(iv) Finally HMG agreed with BAe that the precise timing of the payment of the £150m consideration would follow the clarification of certain tax matters. This delay was time-limited to 31 March 1990.

8 These items were addressed where relevant in Estimates and Reports to Parliament. The Government fully recognised that these additional arrangements were material to the PAC investigation, and from the outset full details were volunteered to the NAO.

9 The Government took the view that these concessions were essentially separate matters consistent with the terms of the Commission's approval. If the EC Commission now wishes to examine them, the Government will be happy to cooperate.

10 I believe that these arrangements were the least that were necessary to secure the successful transfer of the Rover Group to the private sector, which was essential for the future welfare of the Rover Group and those who work in it, as well as being the best deal available for the taxpayer.

dti

the department for Enterprise

The Rt. Hon. Nicholas Ridley MP
Secretary of State for Trade and Industry

Department of Trade and Industry

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Dominic Morris
Private Secretary to the
Prime Minister
10 Downing Street
LONDON
SW1

Direct line 215 5623
Our ref PE2AHO
Your ref
Date 28 November 1989

Dear Dominic

NAO REPORT ON ROVER GROUP

As requested, I attach for the Prime Minister's information:

(i) the text of the National Audit Office's Report on the Sale of Rover Group Plc, being published at 11am;

(ii) the text of the NAO press release;

(iii) the text of the NAO's confidential supplementary memorandum (which will not be published, but which will be in the hands of PAC members).

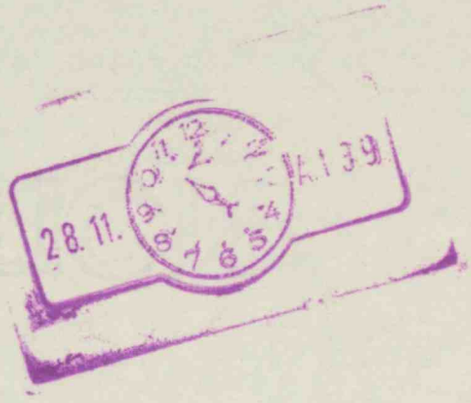
Briefing for Prime Minister's questions this afternoon follows separately.

Yours ever,

Neil Thornton

NEIL THORNTON
Principal Private Secretary

Recycled Paper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SALE OF ROVER GROUP PLC TO BRITISH AEROSPACE PLC

REPORT BY THE COMPTROLLER AND AUDITOR GENERAL

This Report is the property of the National Audit Office.

The Report has been prepared as the basis for an official Report to be presented to Parliament in due course. It is supplied solely for the purpose of verifying the accuracy and completeness of the information contained in it and to obtain views on the conclusions reached.

Neither the Report nor any of its contents should be disclosed to any other person unless such disclosure is authorised by the National Audit Office. The Report must be safeguarded at all times to prevent publication or other improper use of its contents. Unauthorised disclosure may result in legal proceedings.

15.11.89

Rover Group

DEPARTMENT OF TRADE AND INDUSTRY: SALE OF ROVER GROUP PLC TO BRITISH AEROSPACE PLC

SUMMARY AND CONCLUSIONS

Background

1. On 1 March 1988, the Secretary of State for Trade and Industry announced that the Government had entered into exclusive negotiations with British Aerospace plc to sell them the Government's majority shareholding in Rover Group plc. The sale was completed on 12 August 1988 for £150 million, after the Government had made a cash injection of £547 million into Rover Group.

2. This Report records the results of an examination by the National Audit Office (NAO) of the factors influencing the Government's decision to deal exclusively with British Aerospace, of the arrangements for the sale, of their financial implications, and of the achievement of the Government's objectives for the sale.

Findings

3. The main findings and conclusions arising from the NAO's examination were:

On the granting of exclusive negotiating rights to British Aerospace

4. (a) The Government's decision to grant exclusive negotiating rights to British Aerospace up to the end of April 1988 was based on the view that the benefits of competition were outweighed by the risk to Rover Group's prospects arising from the uncertainty that would be associated with a competitive sale. A failure of Rover Group could crystallise the Government's obligations to the Company's creditors under assurances given to Parliament. Ministers had been fully informed of the advantages and disadvantages of dealing exclusively with British Aerospace. They were also aware of the advice given by Baring Brothers and Co Ltd, the Department's financial advisers on the sale, that it was essential to create a competitive market if confidence was to be achieved that the best terms available were obtained. Barings however recognised the Government's right to decide to give weight to broader considerations (paragraphs 2.3-2.6).

On the negotiation of the financial terms of the sale

5. (a) The announcement of the Government's intention to negotiate exclusively with British Aerospace for two months for the sale of Rover Group prompted approaches from four other companies. The Department of Trade and Industry told them that, if negotiations with British Aerospace did not lead to an agreement, alternative proposals would be considered. In the event the four expressions of interest were not translated into firm offers (paragraph 3.5).

(b) The Department's initial expectation was that, after a cash injection to wipe out financial debt, the net cost to the taxpayer of selling Rover Group might be £500 million. But, following submission of the terms to the European Commission, the balance between cash injection and consideration was reduced to £422 million, including the cost of easing tax restrictions (paragraphs 3.3 and 3.11).

On the price paid

6. (a) It is difficult, in the absence of competition, to determine a fair price for a Rover Group substantially relieved of debt. The Department pointed out that the consideration of £150 million was the most that British Aerospace were prepared to pay (paragraph 4.19).

(b) However it should be recognised that, for £150 million, British Aerospace obtained:

- a going concern whose profit for 1987 was £27.9 million which, on the basis of the price/earnings ratio of 5:1 cited by the Secretary of State, suggests a minimum value of some £140 million (paragraphs 4.5-4.6);

- tax benefits worth between £33 million and £40 million, available to reduce the business's future tax liabilities (paragraph 4.9);

- surplus sites, not required for the running of the business, subsequently

estimated by the NAO's advisors as worth £33.5 million at the time of the sale (paragraph 4.12); and

- holdings in nine associated companies, some of which they could sell without detriment to the rest of the business, and from which in two cases they have already raised £126 million, significantly more than the £48 million - £60 million foreseen at the time of the sale (paragraphs 4.14-4.17)

(c) In the circumstances the question arises as to whether, in negotiation, the Department could have argued for a price higher than £150 million. Or, at least, have sought in negotiation clawback provisions to enable the taxpayer to share the benefits arising from the sale of surplus land and associated company holdings; and the utilisation of tax losses.

(d) While accepting the problems in second-guessing the results of negotiations with hindsight, the fact remains that the Department's negotiating

resulted in British Aerospace paying £150 million for a business which made a profit before interest and tax of £65 million in 1988 (paragraph 4.7); and which also had surplus assets and other benefits worth at least £250 million, of which it has so far realised £126 million (paragraphs 4.9, 4.12, 4.15, 4.17). The NAO believe that these figures suggest that the Department could have raised in their negotiations the scope for clawback provisions to enable the taxpayer to share in these significant benefits without prejudice to the Government's objectives for this sale (paragraph 1.8). However, the Department were convinced that this could not have been achieved without cost. They argued that the deal was structured on the basis of British Aerospace assuming the risks as well as the opportunities: if the latter had been curtailed through clawback, it would have fundamentally altered the balance of the terms.

On the achievement of the Government's objectives for the sale

7. The NAO concluded that the Department had substantially met three of the four objectives set

by the Government for the sale of Rover Group, ie:

(a) To privatise Rover Group within the lifetime of the current Parliament. This objective was successfully fulfilled (paragraph 5.2).

(b) To relieve the taxpayer of potential liabilities on the best possible terms. Successive Secretaries of State had given assurances in Parliament that Rover Group would not be left in a position where they could not meet their obligations to creditors. British Aerospace have provided an indemnity against any such reasonably foreseeable claims. However, since the sale price was well below the NAO's valuation of the company at the time of the sale, the NAO questioned the Department's assertion that no better terms could have been secured (paragraphs 5.3-5.6).

(c) To achieve a clean break without further risk to the taxpayer. This objective has been met as far as is practicable. For example, there remain certain monitoring obligations imposed on the Department by

the European Commission (paragraphs 5.7-5.11).

(d) To avoid damage to Rover Group through privatisation. The Company's declared results show that it has been trading profitably since privatisation; indeed profits were substantially higher than forecast in the 1988 Corporate Plan. The Company's 1988 sales were 10 per cent higher than in 1987, although UK market share was not increased (paragraph 5.12).

General Conclusions

8. The NAO recognise that many considerations, other than the purely financial, may come into play when the Government decides to sell state-owned enterprises. And it is not for the NAO to question the policy objectives set in such cases or generally. However two particular issues have arisen from their examination of the Rover Group sale which the NAO recommend should be considered in future sales of Government-owned undertakings.

9. First, it is important, whatever negotiating arrangements are made, for the Government to establish as realistic a valuation as possible of the undertaking to be sold. The NAO acknowledge that the particular circumstances or history of an undertaking may make this difficult but believe that

awareness of this figure would enable the Government to set the price against their assessment of the value of non-financial benefits. The Department told the NAO that, in the circumstances of the sale of Rover Group to British Aerospace, they were convinced that the consideration represented a realistic value which could not have been improved upon.

10. Second, negotiators should carefully examine, and introduce into the negotiations as appropriate, the extent to which the taxpayer's interest would be better served by providing for the public purse to share in the benefits arising from any subsequent sale of surplus assets, or from other sources, rather than seeking a fixed price in which the new owner takes all of any subsequent benefits which materialise. There would, of course, be an offset to a benefit-sharing clause probably in the form of risk-sharing arrangements or a reduction in the fixed consideration payable. The balance between the two forms of sale must therefore be weighed in the individual case and in the light of other policy considerations: there is no guarantee that clawback provisions would give a better result overall. In practice, if the benefit sharing route was adopted, such benefits would need to arise within a reasonable period; and the added value would need to take account of the degree to which it reflected the

efforts of the new owner as distinct from the asset's inherent value at the time of its sale by the Government.

The NAO acknowledge with thanks the help readily given by British Aerospace and the Rover Group in responding to questions and enquiries from the Office on certain aspects of this report.

PART 1: BACKGROUND AND SCOPE OF NAO EXAMINATION

Background

1.1 Rover Group were taken into public ownership in 1975 following acceptance of the Ryder Report by the Government of the day. The British Leyland Motor Corporation, as the Company were then known, were making heavy losses and facing bankruptcy. The Government therefore offered to buy out existing shareholders and subscribed for new shares in the reconstituted company at a total cost of £1.25 billion.

1.2 Currently Rover Group are the largest car manufacturers in the United Kingdom, responsible for 40 per cent of domestic car production and 65 per cent of all car exports. The Group are major employers with 40,500 direct United Kingdom employees and over three times this number in jobs dependent on the Group in the retail, manufacturing and supply sectors.

1.3 Following the sale of Jaguar in 1984, Rover Group returned a number of their other businesses to private ownership while retaining, in some cases, a substantial stake in them. The most significant of these was a 40 per cent holding in DAF, which took over Rover Group's Leyland Trucks and Freight Rover

businesses in 1987; and a 21.7 per cent stake in the Unipart motor components business. The proceeds of these disposals were retained by the Group. These disposals left Rover Group with just two divisions: Austin Rover, the car manufacturer, and Land Rover, specialising in four-wheel drive vehicles.

1.4 Discussions after 1984 between the Government and British Leyland/Rover Group, about returning the remainder of the Company to the private sector, resulted in consideration by the Company and the Department of Trade and Industry of various sale options, including flotation or placement. None of these options was pursued, mainly because of the Government's need to find a solution which would command wide political support and avoid commercially damaging controversy. The Government also felt that a successful flotation would require a marked and sustained improvement in the Company's trading and financial position. The Department considered that such an improvement could not be guaranteed within the lifetime of the current Parliament, the timescale for privatisation agreed between the Company and the Government.

1.5 On 1 March 1988, the Secretary of State for Trade and Industry announced that there would be exclusive negotiations with British Aerospace plc for the Government's 99.8 per cent shareholding in

Rover Group, provided they were concluded by the end of April 1988. An initial deal was concluded by the end of March subject to European Commission approval.

1.6 In the event the sale to British Aerospace was completed on 12 August 1988 at a price of £150 million after the Government had provided a cash injection of £547 million - £469 million in recognition of the Company's debt and £78 million to support its investment programme in the Assisted Areas. British Aerospace subsequently purchased the remaining privately held shares. Table 1 shows that, prior to the sale to British Aerospace, the taxpayer had provided some £2.9 billion in the form of non-interest bearing capital to support the Rover Group since 1975.

1.7 This report records the results of an examination by the National Audit Office (NAO) of the factors influencing the Government's decision to deal exclusively with British Aerospace, of the arrangements for the sale, of their financial implications, and of the achievement of the Government's objectives for the sale.

Table 1

Provision of public funds to Rover Group

	£ million
To implement the Ryder Report recommendations (1975-81)	1,250
To implement the 1981-85 Corporate Plan (1981-84)	980
To support the privatisation of the truck and bus subsidiaries (1987)	680
	2,910

Objectives of the sale

1.8 The Government's objectives in selling Rover Group were:

(a) to complete the privatisation of the Company within the lifetime of the current Parliament;

(b) to relieve the taxpayer of the liability represented by assurances, known as the Varley-Marshall-Joseph assurances, given in the House of Commons by various Secretaries of State that the Government would not allow Rover Group to be left in a position where it would not be able to meet its obligations to creditors;

(c) to ensure that privatisation represented a clean break without further risk to the taxpayer; and

(d) to avoid damage to the business through the process of privatisation.

1.9 The Department told the NAO that the single most important objective was the liquidation of the Varley-Marshall-Joseph liability and that, associated with this objective, their aim was to obtain the best terms available.

PAC Interest

1.10 The Committee of Public Accounts took a close interest in Rover Group after it was taken into public ownership. They were mainly concerned that the public funds provided to the Company were not being matched by improvements in productivity - Eighth Reports of Sessions 1976-77 and 1977-78 and Sixth Report of 1979-80. In their third Report of 1983-84 the Committee examined the Department's arrangements for supervising and monitoring the Company and found them broadly satisfactory.

Scope of the NAO examination

1.11 The NAO examined the following main issues:

- the factors informing the decision to grant exclusive negotiating rights to British Aerospace (Part 2);

- the basis on which the financial terms of the sale were agreed (Part 3);

- the price paid by British Aerospace (Part 4); and

- whether the Department met the Government's objectives for the sale (Part 5).

1.12 In addition to examining the Department's records and discussing with departmental officers the events leading to the sale, the NAO obtained advice on taxation matters from Touche Ross, Chartered Accountants; and on the value of surplus sites from G L Hearn and Partners, Chartered Surveyors; and sought comments on the draft report from Professor Garel Rhys of the University of Wales College of Cardiff, an expert on the motor industry and adviser to the Select Committee on Trade and

Industry. The Rover Group also provided information to the NAO on site values.

1.13 Some details of the sale are commercially sensitive and are being submitted separately to the Public Accounts Committee in a confidential memorandum.

PART 2: NEGOTIATING ARRANGEMENTS

2.1 This Part describes the rationale behind the decision to grant exclusive negotiating rights for the sale of Rover Group to British Aerospace.

Events leading to exclusive negotiations

2.2 On 1 February 1988, the Rover Group Chairman informed the Department of Trade and Industry that he had received an expression of interest in Rover Group from British Aerospace. He expected British Aerospace to make their involvement conditional on exclusive negotiating rights. British Aerospace confirmed this conditional interest later that month.

2.3 The Chairman considered that exclusivity would be in Rover Group's best interest. He was concerned that open competition would give rise to uncertainty that would be commercially damaging. Such uncertainty had arisen early in 1986 because of the negotiations then under way with General Motors and Ford for the sale of the Group's commercial vehicle and car businesses respectively.

2.4 The Department considered that competition would put the Government in a better negotiating position with potential buyers and might lead to more

advantageous sale terms. Nevertheless, they agreed that competitive bidding would lead to uncertainty and damage Rover Group's prospects, such that the Government might have to meet the Group's liability under the Varley-Marshall-Joseph assurances (paragraph 1.8b). Legal advice received by the Department stated that the granting of exclusive negotiating rights to British Aerospace should amount to no more than a statement of intent to deal exclusively. This would leave the Department free to take into account any offers they might receive from other potential bidders when they came to take a final decision on British Aerospace's offer.

2.5 The Department were also aware that other potential buyers were likely to be politically controversial and that speculation about their intentions might be commercially damaging. They therefore consulted Ministers about British Aerospace's bid for exclusive negotiating rights, advising them of the advantages and disadvantages of exclusivity. Ministers agreed that there should be exclusive terms, but for a limited period only.

2.6 Baring Brothers and Co Ltd, the Department's financial advisers on the Rover Group privatisation since 1985, confirmed their earlier preference for limited competitive tender for the sale. Barings argued that it was essential to create a competitive

market if any confidence was to be achieved that the best terms available would be obtained. But they recognised the Government's right to decide to give weight to broader considerations (paragraph 2.5).

2.7 On 1 March 1988 the Secretary of State for Trade and Industry announced that British Aerospace had been given exclusive rights to negotiate for the Government's majority shareholding in Rover Group, providing the negotiations were concluded by the end of April. If not, he would be free to look at other options.

PART 3: FINANCIAL TERMS OF THE SALE

3.1 This Part examines the initial agreement with British Aerospace on the terms of sale, the subsequent referral of these terms to the European Commission, and the terms finally agreed. A summary of the financial terms at each stage of the negotiations is at Annex 1.

February 1988 negotiations

3.2 When, in February 1988, British Aerospace confirmed their interest in buying Rover Group (paragraph 2.2), the Department of Trade and Industry sought to clarify their proposals. British Aerospace were prepared to acquire the Company in return for a net cash injection by the Government of £750 million to write-off the Group's debts. Barings advised the Department that, for negotiating purposes, a debt-free Rover Group could be argued to be worth £950 million - £400 million for Austin Rover, £250 million for Land Rover and £300 million for Rover Group's accumulated tax losses. But, to reflect the risks associated with the business, Barings suggested that the Government's opening negotiating position should be a net cash injection of £250 million - £750 million to write-off the Company's debts in exchange for a payment by British Aerospace of £500 million.

3.3 The Department considered this a useful opening bid but accepted that they might have to settle for a net cash injection of £500 million - £750 million to write-off the debts less £250 million from British Aerospace. This would recognise the limited value of the trading tax losses, which could not be set against profits outside the vehicles sector, and the uncertain prospects of Austin Rover. Ministers agreed that the Secretary of State should attempt to negotiate a deal with British Aerospace at a net cost of up to £500 million.

3.4 However, this proved insufficient to secure the sale. Following further consideration by Ministers and renewed negotiations, the Secretary of State and British Aerospace agreed indicative terms under which the Government would inject £800 million to write off debts and British Aerospace would pay £150 million for a debt free Rover Group - a net cost to the taxpayer of £650 million.

Other expressions of interest

3.5 Despite the Government's announced intention to negotiate exclusively with British Aerospace for a period of two months, approaches were made by four other interested parties. In the light of the legal advice they had received (paragraph 2.4), the

Department pointed out that they had agreed to grant British Aerospace a period of exclusive negotiating rights. If these negotiations did not lead to an agreement, alternative proposals would be considered. In the event none of these other expressions of interest was translated into a firm offer.

Exclusive negotiations

3.6 The Department's main concern was that British Aerospace should not sell Rover Group during the first five years of ownership. They therefore proposed that British Aerospace would repay the net benefit of ownership and sale up to a limit of £650 million - the value of the net cash injection proposed in the original terms (paragraph 3.4) - if they relinquished control of principal Rover Group trade marks or any substantial part of the business without the Department's prior approval. The sale of shares in other businesses or of surplus sites was not covered by these conditions.

3.7 The draft Sale and Purchase Agreement also provided: that any benefit to British Aerospace of their use of Rover Group's trading tax losses where those losses exceeded £500 million should be repaid, effectively neutralising £1,100 million of Rover Group's accumulated tax losses; that the benefit of

Rover Group's capital tax losses and allowances should be restricted to Rover Group activities and would not be available to British Aerospace as a whole; and that British Aerospace would reimburse the Government should any payments become due under the Varley-Marshall-Joseph assurances (paragraph 1.8(b)).

Reference to the European Commission

3.8 Members of the European Community require the approval of the European Commission before granting state aid to industry, to ensure that companies thus assisted do not gain an undue advantage over their competitors. The terms of the proposed sale of Rover Group were therefore referred to the Commission in March 1988. Because of the real possibility of distortion of competition in the motor vehicle industry in Europe, the Commission decided to investigate the sale.

3.9 Such investigations are normally lengthy but the Government stressed the need for a quick decision. They were concerned that a long period of uncertainty would hamper the ability of Rover Group's management to take key decisions and be commercially damaging to the Company.

3.10 The Commission rejected the Department's proposal that a write off of £800 million was necessary to eliminate total indebtedness (paragraph 3.4). The Commission's view was that some £231 million of this sum would be used to provide working capital rather than to meet debts. Moreover, to write off the whole of the debt would put Rover Group in a more favourable financial position than most of their competitors. The Commission therefore considered that a minimum debt of £100 million should be retained by Rover Group, leaving the Government to provide £469 million.

3.11 Although the Government alone was responsible for negotiating with the European Commission, Rover Group and British Aerospace were kept informed of progress. It soon became clear that a reduction in the cash injection to the level proposed by the Commission would jeopardise the whole deal. Following Government representations, the Commission agreed that the gap might be bridged by providing regional aid of some £78 million and by easing the restrictions on the use of Rover Group's capital tax losses and allowances (paragraph 3.7), estimated by the Commission to be worth £25 million. The Government considered that these terms (summarised in Table 2) were likely to be the best that could be obtained from the Commission. They were formally approved by the Commission on 13 July 1988.

Table 2

Terms approved by the European Commission

	£ million
Debt write-off	469
Regional Assistance	78
Easing of tax restrictions	25
(Commission estimate)	572
Less: payments by British Aerospace	150
	422

Honda agreement with British Aerospace

3.12 On 13 July 1989 Rover and Honda announced that, as part of a strengthening of their relationship, Honda were to take a 20 per cent stake in Rover Group while Rover Group would take a similar stake in Honda's United Kingdom manufacturing company. This agreement in principle was announced after the NAO's inquiries had been completed, but remains subject to the conclusion of binding legal agreements later this year.

PART 4: THE PRICE PAID

4.1 This Part of the report examines how far the value of Rover Group, at the time of the sale, was commensurate with the £150 million paid by British Aerospace for a business that was substantially relieved of debt. It also considers subsequent developments affecting the value of the business.

4.2 As described in paragraph 1.3, by 1987 Rover Group had been reduced to two divisions - Austin Rover and Land Rover - and held a number of minority stakes in former subsidiaries. Although some of the potential buyers (paragraph 3.5) had earlier expressed interest in acquiring the two businesses separately, the Department of Trade and Industry decided to negotiate with British Aerospace for the sale of the business as a whole; and the Government insisted that Rover Group should remain intact for at least five years. The NAO therefore concentrated on the value of Rover Group as a going concern.

4.3 The NAO decided that the elements relevant to such a value included any accumulated tax benefits, and the value of any significant assets surplus to the requirements of the main business, such as sites and shareholdings in associated companies.

Value of the business as a going concern

4.4 The market value of a business is ultimately what a willing buyer is prepared to pay in the face of competition. As there was no competition in this case, the NAO examined other indicators of Rover Group's intrinsic worth. Barings' initial advice to the Department (paragraph 3.2) was that a debt-free company could be argued for negotiating purposes to be worth £950 million: £400 million for Austin Rover plant based on a hypothetical, similar investment on a green field site; £300 million for tax losses; and £250 for Land Rover based on forecast 1988 profits. However Barings recognised that this value of £950 million would have to be substantially discounted in view of the risks associated with the business.

4.5 As part of their investigation of the sale (paragraphs 3.8-3.11), the European Commission concluded that Rover Group's true value appeared to be about £950 million, inclusive of their land and buildings, assets, stakes in other companies, and tax benefits (paragraph 4.8-4.9). However, the Secretary of State pointed out that no purchaser could realise the Company's assets without incurring redundancy costs of £550 million or more. He also explained that the consideration of £150 million was

consistent with a price/earnings ratio of 5:1, in line with conventional practice.

4.6 At that time Rover Group had just announced 1987 group profits, before interest and tax, of £27.9 million. Although this represented the best trading performance for nine years it was, at just one half per cent of turnover, very sensitive to variations in turnover. Nevertheless, it was in line with Rover Group's 1988 Corporate Plan which was forecasting increasing profits. Applying the price/earnings ratio of 5:1 to Rover Group's 1987 profit of £27.9 million suggests a minimum value for the Company of some £140 million.

4.7 Rover Group's profit before interest and tax of £65 million in 1988 was a considerable improvement over the 1988 Corporate Plan forecast, which suggested an improving financial trend over that forecast in the Plan. It was also an improvement on the 1987 profit, but the Department pointed out that it needed to be seen in the context of a year in which Ford UK, Peugeot-Talbot UK, and Vauxhall all made improved profits, the latter two on much lower turnover.

Tax benefits

4.8 In addition to the value of Rover Group's future profit potential, the value of any accumulated tax benefits at the date of sale must be taken into account. In the case of the Rover Group these benefits will arise from three main sources:

- trading losses at the date of sale which may be offset against the Corporation Tax liability arising on future Rover Group profits; however the losses to be treated in this way are limited to £500 million (paragraph 3.7).

- accumulated losses from past capital transactions may be offset against future liabilities for Capital Gains tax.

- the Group had not claimed all their entitlement to capital allowances which reduce a company's tax liability by reference to the depreciation of certain capital assets; such allowances are available for use in later years.

4.9 It is difficult to put a precise value on these tax allowances since much depends on finalising past years' tax liabilities and on Rover Group's future

profits. At the time of the negotiations with the European Commission, the Department noted that the absolute maximum cash value of these allowances might be in the range £265-345 million (Table 3). The Department's legal consultants advised that a substantial discount would need to be applied to reach a net present value but did not say by how much. The NAO therefore commissioned the taxation division of Chartered Accountants, Touche Ross, to calculate the potential value to British Aerospace of Rover Group's tax benefits at the time of the sale. Touche Ross estimated this value at between £33 million and £40 million (Annex 2). They also considered that it would have been reasonable and preferable from a commercial viewpoint to have included a clause in the sale agreement whereby the benefit of both the trading losses and the capital losses is shared by the purchaser and the vendor when the losses are realised. However, such an arrangement is not usual - smaller sums are commonly involved in such cases - and the Department questioned whether such an arrangement would have been preferable in this instance.

Table 3

Value of Rover Group's Tax Benefits

	£ million
Trading Tax Losses	175
Capital Losses	70
Unclaimed Capital Allowances	20-100
	265-345

Value of surplus sites

4.10 The Secretary of State told the Trade and Industry Committee on 18 May 1988 that no valuation had been carried out of Rover Group's sites and other assets though, of course, they had a book value in the accounts. Since the value attributed to the Company's land and buildings by British Aerospace was not tested by competition (paragraph 2.4), the NAO asked Rover Group whether they could provide an independent assessment of the existing and alternative use values of each of their sites, and of those likely to become surplus, at the time of the sale.

4.11 In response, Rover Group provided the NAO with details of a valuation by G L Hearn and Partners, Chartered Surveyors, commissioned by British Aerospace. This showed that as at 31 December 1988 the existing use value of all Rover Group sites,

excluding Bathgate which Rover Group had sought permission (since refused) to develop as a retail and leisure centre, was £514.4 million, of which £21.6 million was for the surplus ones.

4.12 In the absence of open market values for an alternative use, the NAO commissioned G L Hearn and Partners to assess such values for the surplus sites (including Bathgate) at the time of the sale. They reported that these values were likely to have totalled £33.5 million (Annex 3). This valuation was on the assumption that there were no unusual or onerous cost implications in respect of the demolition of buildings or the removal of plant and machinery. It made no allowance for the indirect rationalisation costs of making sites currently in productive use available for disposal.

4.13 No provision was made in the Sale and Purchase Agreement for the Government to clawback any part of the profits on the sale of surplus sites.

Value of shareholdings in associated companies

4.14 At the time of the sale, Rover Group held stakes in nine associated companies with a total book value of £100.6 million. To the extent that the return on these holdings is reflected in Rover Group profits, their value is also reflected in the

value for the Company suggested at paragraph 4.6. But again, since their value was not tested by competition, the NAO sought to determine whether it was properly reflected in the sale price.

DAF

4.15 Barings advised the Department that, in the context of a break-up sale of a company not then listed on a stock exchange, the Rover Group's 40 per cent holding in DAF might be worth some £40 million - £50 million. This was on the basis of DAF's total 1987 profits of £17.9 million and an historic price:earnings ratio of 6:1, in line with ratings of similar companies at that time. Barings noted that the Group's 1988 Corporate Plan assumed the Rover Group's holding would be sold in 1990 for £90 million. This latter valuation for the whole stake has since proved to be a very conservative estimate. In May 1989, following the flotation of DAF on the London and Amsterdam stock exchanges, Rover Group relinquished 60 per cent of their holding for £87 million, net of sale costs. Their retained holding in DAF was worth a further £60 million at the flotation price, giving a total value of the Rover Group's original holding in DAF of £147 million less than a year after the sale to British Aerospace.

4.16 More than a year had elapsed between Barings' valuation and the flotation, and the increase reflects any changes in the European truck market and the effect of this on DAF's profits and on the industry's market rating, as well as DAF's transition from unlisted to listed status.

Istel

4.17 Since the sale, Rover Group have also agreed to sell their holding in Istel for £39.1 million, compared with Baring's estimate of £8 million - £10 million.

NAO Conclusions

4.18 Having regard to the above factors the NAO ascribed the following values to Rover Group:

(a) £140 million, on the basis of Rover Group's 1987 profits (paragraph 4.6).

(b) £33 million - £40 million, being the benefit to British Aerospace of Rover Group's accumulated tax losses and allowances, as assessed by Touche Ross, Chartered Accountants commissioned by the NAO (paragraph 4.9).

(c) £33.5 million, being the alternative use value of the Rover Group sites surplus to the requirements of their main business, as assessed by G L Hearn and Partners, Chartered Surveyors commissioned by the NAO (paragraph 4.12).

On the basis of the above the NAO assess the total value of the Rover Group to have been at least £206.5 million at the date of sale. In addition, they note that the book value placed on the Group's holdings in subsidiary companies was £100.6 million (paragraph 4.14). This is already reflected at (a) above but, since the worth of these holdings represents such a high proportion of the overall value, it suggests that the value based on Rover Group earnings is very much a minimum figure.

4.19 However, the NAO recognise the impossibility, in the absence of competition based on a full knowledge of all relevant facts, of determining with any great accuracy a fair price in March 1988 for a substantially debt-free Rover Group. The Department are convinced that the consideration represented the most that British Aerospace were prepared to pay. In their view, it was the only way of enabling the deal to proceed and of avoiding a renewed period of damaging uncertainty about Rover Group's future (paragraph 2.3). Nevertheless, in the light of values

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PART 5: ACHIEVEMENT OF THE GOVERNMENT'S OBJECTIVES

5.1 This Part examines the extent to which the Department met the Government's four objectives for the sale of Rover Group (paragraph 1.8).

(a) To privatise Rover Group within the lifetime of the current Parliament.

5.2 The completion of the sale to British Aerospace in August 1988 represented the successful fulfilment of this objective.

(b) To relieve the taxpayer of the liability represented by the Varley-Marshall-Joseph assurances (paragraph 1.8(b)), while securing the best possible terms for the sale of Rover Group.

5.3 Although the precise legal standing of these assurances remains untested, the Company's creditors would have been influenced by them and been aware that the Government would probably have stood by them. The Department estimated this contingent liability at some £1.6 billion at 31 March 1988.

5.4 On 29 March 1988, the Government announced that, from the date of completion of the sale, no new obligations would be covered by the assurances. New

obligations entered into after that date would no longer be so covered beyond completion.

5.5 The Government left their own position on obligations entered into before 31 March 1988 unchanged, but negotiated an indemnity from British Aerospace against payments under the assurances in respect of such obligations remaining outstanding six months after completion of the sale. The Department considered that no other Rover Group obligations, beyond those listed in the schedule of obligations covered by the indemnity, were likely to mature and give rise to a claim under the assurances. These arrangements effectively extinguished the Government's Varley- Marshall-Joseph obligations six months after the sale of Rover Group.

5.6 The Department therefore succeeded in relieving the taxpayer of the Varley-Marshall-Joseph assurances. However since, for the reasons given in Part 4, the sale price was markedly less than the Group's value, in the NAO's view there are some grounds for believing that the Department did not achieve their parallel aim of obtaining the best available terms.

(c) To achieve a clean break without further risk to the taxpayer

5.7 The Department's intention was to detach the management of Rover Group from non-commercial influences and to subject them to full market disciplines; and to avoid exposing the taxpayer to residual risk in the event of the business getting into difficulty. However there are continuing Government commitments to the Rover Group as follows.

Fulfilment of the Rover Group 1988 Corporate Plan.

5.8 The European Commission's approval of the sale (paragraph 3.11) was conditional on British Aerospace's fulfilment of the Rover Group 1988 Corporate Plan. Failure to do so could result in the repayment by British Aerospace of some or all of the cash injected by the Government into the Company. British Aerospace were concerned that this would limit their freedom to manage Rover Group but, following a report of consultations between the Government and the Commission on this point, were reassured that the Department would be obliged to seek repayment only for significant and unjustified departures from the Plan. To this end the Government is obliged to provide the Commission with half-yearly reports. Thus a clean

break has not been achieved, although this constitutes no residual risk to the taxpayer.

Regional assistance.

5.9 To facilitate the sale, the Department provided Rover Group with £78 million in the form of regional assistance (paragraph 3.11). The European Commission required the grant to be tied to Rover Group's investment programme in the assisted areas, as derived from their 1988 Corporate Plan. The Department are required to monitor and report to the Commission on this expenditure. Again, although there has not been a clean break, there is no residual risk to the taxpayer.

Varley-Marshall-Joseph assurances.

5.10 The possibility that the Department will be required to meet any Rover Group obligations not covered by the British Aerospace indemnity (paragraph 5.5) is remote.

5.11 The Department have thus effectively met the objective of achieving a clean break, except for certain monitoring responsibilities imposed by the European Commission.

(d) To avoid damage to Rover Group through privatisation

5.12 The granting of exclusive negotiating rights to British Aerospace was designed to avoid a prolonged period of uncertainty which might damage Rover Group's prospects. The 1988 profits were substantially above those forecast in the 1988 Corporate Plan. And in 1988 Rover Group achieved 10 per cent higher retail sales in the United Kingdom compared with 1987 - albeit in a record high domestic market. These results suggest the objective was achieved.

15.11.89

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SUPPLEMENTARY MEMORANDUM BY THE COMPTROLLER AND AUDITOR GENERAL

DEPARTMENT OF TRADE AND INDUSTRY: SALE OF ROVER GROUP PLC TO BRITISH AEROSPACE PLC

Introduction

1. My Report on the National Audit Office's examination of the sale of the Government's shareholding in Rover Group to British Aerospace is published in HC xxx. The Department of Trade and Industry (DTI) have represented to me that publication of certain information relating to the sale could seriously undermine the competitive position of Rover Group and British Aerospace in international markets. This Memorandum provides details of this information and certain other details which the Department have asked to be treated as confidential, including the identities of certain third parties. The Department consider that

it could be prejudicial to future relations with private sector bodies if such bodies were to believe that confidential approaches might subsequently be disclosed without their consent.

Other expressions of interest (paragraph 3.5)

2. The four other parties who expressed an interest in buying Rover Group during the Department's negotiations with British Aerospace were: Ford of Europe, Volkswagen, Lonrho (acting in partnership with Toyota), and Melton Medes, a Nottinghamshire company. As indicated in my Report, none of these expressions of interest was translated into a firm offer.

Final negotiations between the Department and British Aerospace (paragraphs 3.10 and 3.11)

3. Paragraph 3.10 of my Report notes the decision of the European Commission that the DTI proposed cash injection of £800 million to write-off Rover Group's debts should be reduced to £469 million. Although the agreement to provide £78 million of regional assistance and to ease the restriction on the use of tax benefits (which British Aerospace privately acknowledged would probably be worth closer to £35 million rather than £25 million as estimated by the Commission) (paragraph 3.11) partly

offset the reduction, British Aerospace were not prepared to accept these terms. After further negotiations between them and the Department, the following terms were agreed, in addition to those approved by the Commission:

(a) The Department would reimburse up to £9.5 million of British Aerospace's acquisition costs including those incurred in the purchase of the minority's shares.

(b) The Department would also reimburse £1.5 million of Rover Group's costs incurred in facilitating the sale of the Government's shareholding.

(c) Payment of the £150 million purchase price would be deferred until the resolution of certain tax matters, but in any event, not later than 30 March 1990. At the time of the sale the Department estimated the value of this concession to British Aerospace at about £22 million.

(d) The Department agreed to British Aerospace withdrawing its offer of a £5 million contribution to the Columbus project, administered by the European Space Agency. This sum will now be paid by the Department.

4. The value of the additional concessions at (a) to (d) above was about £38 million, increasing the net cost to Government of the final sale terms from £422 million (paragraph 3.11 of my Report) to £460 million.

5. In addition, as a result of the reduction in the cash injection imposed by the Commission, the Department agreed to reduce the maximum repayment by British Aerospace if they sold Rover Group within five years from £650 million (paragraph 3.6 of my Report) to £400 million.

Profit forecast in Rover Group's 1988 Corporate Plan (paragraph 4.6)

6. Paragraph 4.6 of my Report refers briefly to the prospect of increasing profitability of the Group. Rover Group's 1988 Corporate Plan forecast profits before interest and tax were as follows:-

	£ million
1988	37.5
1989	52.4
1990	103.8
1991	90.8
1992	142.5

7. The Department stressed that at the time of the sale Rover Group's ability to deliver this improvement in profitability was subject to risks. These included the market reaction to new models; the then lack of a long term collaboration commitment from Honda; exchange rate fluctuations, particularly affecting sales in the United States and purchases from Japan; and the likely return to greater competition in the domestic market in an industry particularly exposed to cyclical influences. So far Rover Group's improvement in profitability is on course; however its market share relative to other manufacturers has slipped back, and the success of the Company's vitally important new product strategy, entailing a £1 billion capital expenditure programme, has still to be proved.

Value of surplus sites (paragraph 4.12 and Annex 3)

8. Paragraph 4.12 of my Report refers to professional valuations of surplus Rover Group sites commissioned by the NAO. The sites in question, and their respective open market values as at 1 May 1988, were:

	£ million
a) Cowley South, Oxford	20.0
b) Bathgate, West Lothian, Scotland	5.0
c) Llanelli, South Wales	0.5

d) Drews Lane, Birmingham 8.0

33.5

Value of shareholdings in associated companies
(paragraphs 4.14-4.17)

9. Paragraph 4.14 of my Report refers to the total net book value of Rover Group's associated companies. At the time of the sale Barings estimated the potential realisable value of these companies at between £109 million - £144 million (Table 1). This estimate was of a break-up valuation based generally on the application of price/earnings ratios to then-current earnings. Barings noted that the net realisable value may have been towards the lower end of this range since the ratios used related to listed companies, whereas all these investments except Land Rover Santana were unquoted. In the case of that company, the valuation was based on the then price of the stock on the Spanish Stock Exchange. However, Rover Group do not believe that such a value would have been achieved as there had been little trading in this stock which is predominantly held in large blocks.

Table 1

Value of Rover Group's shareholdings in associated companies

Company	Book Value £ million	Estimated Realisable Value £ million
DAF BV	66.4	40-50
Unipart	17.0	15-20
Land Rover Santana	6.6	30-40
Wholesale Vehicle Finance Ltd	3.3	4-6
Istel Holdings Ltd	3.0	8-10
JRA Holdings Ltd	2.2	2-3
Llanelli Radiator Holdings Ltd }		
Austin Rover Finance Ltd }	2.1	10-15
Austin Rover Cars of N America }	—	—
	100.6	109-144

15. [redacted]

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DRAFT PRESS NOTICE

REPORT BY THE COMPTROLLER AND AUDITOR GENERAL: DEPARTMENT OF TRADE AND INDUSTRY: SALE OF ROVER GROUP PLC

John Bourn, head of the National Audit Office today reported to Parliament the results of an examination by the National Audit Office of the sale by the Department of Trade and Industry of Rover Group to British Aerospace. The sale was completed on 12 August 1988 for £150 million, after the Government had made a cash injection of £547 million substantially to write off most of the Group's debts. This brought the provision of public funds to Rover Group and their predecessor bodies since 1975 to £3,457 million.

The NAO acknowledge the difficulty in determining an appropriate price for Rover Group, and record the Department of Trade and Industry's view that £150 million was the most that British Aerospace were prepared to pay. Nevertheless, they point out that for that price British Aerospace acquired a business which made a profit before interest and tax of £65 million in 1988; and which also had surplus assets and other benefits worth at least £250 million, of which they have so far realised £126 million.

The NAO identify two particular lessons arising from their examination of the sale of Rover Group for future sales of Government-owned undertakings. One is the importance of establishing as realistic a valuation as possible of the undertaking to be sold. The other is the importance of considering and, where appropriate, of negotiating the inclusion of a contract provision for sharing the benefits of subsequent disposals of assets between taxpayer and purchaser. The NAO recognise that clawback is not always advantageous, since it will affect the balance of the terms. The point is that it should be properly explored and evaluated.

The Report records that the Government's decision to grant exclusive negotiating rights to British Aerospace was based on the view that the benefits of competition were outweighed by the risk to Rover Group's prospects arising from the uncertainty that would be associated with a competitive sale. The announcement of the Government's intention to negotiate exclusively with British Aerospace prompted approaches from four other companies but these were not translated into firm offers.

The NAO conclude that the Department had substantially met three of the four objectives set by the Government for the sale: to privatise Rover Group within the lifetime of the current Parliament; to achieve a clean break from the Group without further risk to the tax payer; and to avoid damage to the Group through privatisation.

The fourth and most important objective for the sale was to relieve the taxpayer of potential liabilities for Rover Group on the best possible terms. This objective was partly met in that British Aerospace have provided an indemnity against reasonably foreseeable claims; but while it is not always reasonable to "second guess" negotiations with hindsight, the sale price was well below the NAO's valuation of Rover Group at the time of the sale. The Department's view is that, in the circumstances of the sale of Rover Group to British Aerospace, the consideration represented a realistic value and the terms of disposal could not have been improved upon.

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cc. Rover Group for info.

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FRAME INDUSTRIAL

SALE OF ROVER GROUP

SUMMARY

1. DTI OFFICIALS AND THE COMMISSION HELD A USEFUL INFORMATION EXCHANGE TODAY IN WHICH WE EXPLAINED FURTHER BACKGROUND TO THE SALE OF ROVER GROUP TO BRITISH AEROSPACE, AND UNDERLINED OUR WILLINGNESS TO COOPERATE FULLY WITH COMMISSION. COMMISSION SIDE MADE CLEAR THAT NO DECISONS WERE LIKELY BY THEM UNTIL THE NEW YEAR.

DETAIL

2. DTI OFFICIALS (LED BY MISS NEVILLE-ROLFE AND MR COCHLIN) MET TODAY DGIV (SUNNEN AND OTHERS) AND SIR LEON BRITTAN'S CABINET (CATHERINE DAY) TO EXPLAIN THE FURTHER BACKGROUND TO THE SALE OF ROVER GROUP TO BRITISH AEROSPACE, AND TO HAND OVER FULL INFORMATION.

3. DTI BEGAN BY EXPLAINING THE TIMETABLE AND CONTEXT OF THE FOUR FURTHER ITEMS AGREED WITH BRITISH AEROSPACE IN JULY 1988 BUT NOT DISCLOSED TO THE COMMISSION AT THAT TIME. WE EXPLAINED THAT THE GOVERNMENT TOOK THE VIEW THAT THESE CONCESSIONS WERE ESSENTIALLY SEPARATE MATTERS CONSISTENT WITH THE TERMS OF THE COMMISSION'S APPROVAL. THEY WERE NOT INTENDED TO BE SECRET, AND REFERENCES TO THEM HAD BEEN MADE IN STATEMENTS TO PARLIAMENT. IN OUR VIEW, WHILE GIVING A BENEFIT TO BRITISH AEROSPACE, THEY DID NOT HAVE AN IMPACT ON ROVER, AND THEREFORE DID NOT HAVE A DISTORTING EFFECT ON COMPETITION WITHIN THE VEHICLES SECTOR IN THE EC. HOWEVER IF THE COMMISSION WISHED TO EXAMINE THEM WE WOULD BE HAPPY TO COOPERATE FULLY. TO THIS END WE HAD ALREADY GIVEN THE COMMISSION THE INFORMATION IN THE NATIONAL AUDIT OFFICE REPORT AND THE COMPTROLLER AND AUDITOR GENERAL'S CONFIDENTIAL MEMORANDUM, AND WOULD BE HAPPY TO GIVE DGIV FURTHER CLARIFICATION AND TO RESPOND TO ANY QUESTIONS.

4. CATHERINE DAY UNDERLINED THAT SIR LEON BRITTAN HAD TO DATE TAKEN NO VIEW ON THE CASE. HE WOULD WISH TO DECIDE IN THE LIGHT OF FULL INFORMATION AND DGIV'S ADVICE. THIS WOULD NEED TO COVER BOTH THE EC COMPATIBILITY OF THE NEW ITEMS, AND WHETHER THE COMMISSION

MIGHT HAVE TAKEN A DIFFERENT VIEW IN JULY 1988 IF IT HAD HAD THE FULL INFORMATION NOW AVAILABLE. FOLLOWING DGIV'S REPORT, SIR LEON WOULD WISH TO DISCUSS THE CASE WITH MR RIDLEY. THIS DISCUSSION WAS UNLIKELY TO TAKE PLACE BEFORE JANUARY. SIR LEON BRITTAIN WOULD ALSO PREFER THE PARLIAMENTARY PROCESS IN THE UK, INVOLVING HEARINGS BY THE PUBLIC ACCOUNTS COMMITTEE, TO FINISH BEFORE ANY COMMISSION DECISION. WE EXPLAINED OUR UNDERSTANDING THAT THE PAC WOULD FINISH THEIR HEARINGS AND THE INFORMATION GATHERING STAGE IN JANUARY 1990 ALTHOUGH THEY MIGHT TAKE SOME TIME THEEAFTER TO PRODUCE THEIR REPORT. WE HOPED IT WOULD BE POSSIBLE TO PROCEED WITH COMMISSION DISCUSSIONS IN PARALLEL. MR RIDLEY WOULD LIKE TO REACH A CONCLUSION AS SOON AS POSSIBLE.

5. AS FOR PROCEDURES, MISS DAY SAID THAT SIR LEON BRITTAN WOULD NEED TO INFORM THE COMMISSION AS A WHOLE ABOUT THE CASE. THEY WOULD ALSO NEED TO CONSULT THE COMMISSION LEGAL SERVICES. BUT THEIR PRELIMINARY VIEW WAS THAT DEPENDING ON THE OUTCOME OF DGIV'S INVESTIGATION IT WOULD NOT NECESSARILY BE ESSENTIAL FORMALLY TO REOPEN PROCEEDINGS. MOREOVER DISTINCTION COULD BE DRAWN BETWEEN THE ADDITIONAL ITEMS WHERE THEY THOUGHT IT UNLIKELY THAT A NEW PROCEDURE WOULD NEED TO BE OPENED, AND THE OVERALL DEAL WHERE IT MIGHT BE NECESSARY TO RE-OPEN PROCEDURES IF THE COMMISSION DECIDED TO RE-EXAMINE THE DEAL AS A WHOLE.

6. DISCUSSIONS THEN DIVIDED INTO TWO PARTS, WITH THE COMMISSION FIRST SEEKING CLARIFICATION ON THE FOUR ITEMS NOT HITHERTO DISCLOSED, AND SECOND ON THE DEAL MORE GENERALLY PICKING UP POINTS AND PRESS REPORTS ABOUT ITS EXCLUSIVITY, THE VALUATION OF THE GROUP, AND PROFIT AND CASH FLOW FORECASTS. (MISS CARTER CVM WILL DO A FULL RECORD). WE CONCLUDED THE MEETING BY HANDING OVER ALL THE INFORMATION PREVIOUSLY REQUESTED BY THE COMMISSION AND UNDERLINING OUR WILLINGNESS TO RESPOND TO ANY FURTHER QUESTIONS THEY HAD.

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DRAFT PRESS NOTICE

REPORT BY THE COMPTROLLER AND AUDITOR GENERAL:
DEPARTMENT OF TRADE AND INDUSTRY: SALE OF ROVER GROUP PLC

John Bourn, head of the National Audit Office today reported to Parliament the results of an examination by the National Audit Office of the sale by the Department of Trade and Industry of Rover Group to British Aerospace. The sale was completed on 12 August 1988 for £150 million, after the Government had made a cash injection of £547 million substantially to write off most of the Group's debts. This brought the provision of public funds to Rover Group and their predecessor bodies since 1975 to £3,457 million.

The NAO acknowledge the difficulty in determining an appropriate price for Rover Group. They point out that for £150 million British Aerospace acquired a business which made a profit before interest and tax of £65 million in 1988; and which also had surplus assets and other benefits worth at least £250 million, of which they have so far realised £126 million. They record the Department of Trade and Industry's view that £150 million was the most that British Aerospace were prepared to pay, and that in acquiring the business British Aerospace assumed risks as well as opportunities.

The NAO identify two particular lessons arising from their examination of the sale of Rover Group for future sales of Government-owned undertakings. One is the importance of establishing as realistic a valuation as possible of the undertaking to be sold. The other is the importance of considering and, where appropriate, of negotiating the inclusion of a contract provision for sharing the benefits of subsequent disposals of assets between taxpayer and purchaser. The NAO recognise that clawback is not always advantageous, since it will affect the balance of the terms. The point is that it should be properly explored and evaluated.

The Report records that the Government's decision to grant exclusive negotiating rights to British Aerospace was based on the view that the benefits of competition were outweighed by the risk to Rover Group's prospects arising from the uncertainty that would be associated with a competitive sale. The announcement of the Government's intention to negotiate exclusively with British Aerospace prompted approaches from four other companies but these were not translated into firm offers.

The NAO conclude that the Department had substantially met three of the four objectives set by the Government for the sale: to privatise Rover Group within the lifetime of the current Parliament; to achieve a clean break from the Group without further risk to the tax payer; and to avoid damage to the Group through privatisation.

The fourth and most important objective for the sale was to relieve the taxpayer of potential liabilities for Rover Group on the best possible terms. This objective was partly met in that British Aerospace have provided an indemnity against reasonably foreseeable claims; but while it is not always reasonable to "second guess" negotiations with hindsight, the sale price was well below the NAO's valuation of Rover Group at the time of the sale. The Department's view is that, in the circumstances of the sale of Rover Group to British Aerospace, the consideration represented a realistic value and the terms of disposal could not have been improved upon.

NOTE FOR EDITORS

The Committee of Public Accounts will take evidence on the Report and on a confidential memorandum covering commercially sensitive information relating to the sale on 4 December.

The Comptroller and Auditor General, Mr John Bourn, is the Head of the National Audit Office employing some 900 staff. He, and the NAO, are totally independent of Government. He certifies

the accounts of all Government Departments and a wider range of other public sector bodies; and he has statutory authority to report to Parliament on the economy, efficiency and effectiveness with which department and other bodies use their resources.

All enquiries to NAO Press Office: Tel: 01-798 7400

RESTRICTED

10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

6 November 1989

GENERAL MOTORS

Thank you for your letter of 2 November enclosing a draft of a possible letter from the Prime Minister to Roger Smith, the Chairman of General Motors.

The Prime Minister has considered the proposal that she should write to Mr. Smith, but concluded this would not be appropriate. She feels the essential point is that the Government's action in waiving the special share was to demonstrate its neutrality as between possible different bidders for Jaguar; were she to write to GM on the basis proposed, it might give the impression that the Government now felt it would have been better not to waive the share at the time this was done.

PAUL GRAY

Mrs. Rosalind Cole,
Department of Trade and Industry.

RESTRICTED

PRIME MINISTER

Nick Ridley is concerned that General Motors may be disenchanted by the Government's actions over the Jaguar Special Share, particularly as this was followed so quickly by the recommended sale to Ford. He is anxious to do what we can to repair relationships with GM, particularly given the possibility of expansion of their facilities in this country. He therefore suggests you might write to the GM Chairman in the terms attached.

You will want to consider whether to do this. The risk in writing seems to me that you might be seen to be protesting too much; with that in mind I have made various amendments to the original DTI draft. As it now stands I think it probably would be worth your writing to Mr. Smith.

Content to sign? - No

But we were neutral on the matter. It was Jaguar / Ford who took such advantage. I. N.R. now saying it would have been better NOT to release the share when we did?

Reg.

(PAUL GRAY)

3 November 1989

jaguar.dca

10 DOWNING STREET

THE PRIME MINISTER

I know that you were greatly disappointed by the Government's announcement of its intentions in relation to its Special Share in Jaguar.

I should like personally to reassure you that our decision was not in any sense intended to reflect a particular Government view on the future ownership of the company; we have been and remain entirely neutral on that issue. As Nicholas Ridley explained to Parliament on 31 October, however, the restrictions on shareholdings entrenched by the Special Share were causing uncertainties about the company's future by prompting speculation over how these powers would be exercised. This in turn was distorting the basis on which all parties involved had to reach decisions. As the speculation intensified, we felt that the Government's position should be made clear as a matter of urgency. It would have become invidious to have to make such a clarification as events developed.

Let me assure you that the Government values very highly the contribution to the United Kingdom economy made by GM through its various operations in this country. I sincerely hope that we continue to have a constructive dialogue with GM on the future development of these activities.

Mr. Roger B. Smith

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the department for Enterprise

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The Rt. Hon. Nicholas Ridley MP
Secretary of State for Trade and Industry

Paul Gray Esq
Private Secretary to the
Prime Minister
10 Downing Street
LONDON SW1A 2AA

Department of Trade and Industry

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Telex 8811074/5 DTHQ G
Fax 01-222 2629

Direct line 01 215 5622
Our ref PB4ADM
Your ref
Date 2 November 1989

Dear Paul

GENERAL MOTORS

My Secretary of State's announcement of the Government's intentions in relation to the Jaguar Special Share was badly received by General Motors who regarded it as a pro-Ford move which effectively killed off GM's own hopes of a deal with Jaguar based on a minority holding. This morning's joint announcement by Ford and Jaguar will not have eased their concerns.

My Secretary of State is anxious that we should do whatever we can to repair relationships with GM (with whom we have been discussing possible expansion of their car and component activities in the UK). He feels that the most effective course might be for the Prime Minister herself to write to GM Chairman, Roger Smith, clarifying the Government's position and emphasising how much we still value GM's contribution to the UK.

I attach the draft of a letter for the Prime Minister's consideration.

Yours
Rosalind Cole

ROSALIND COLE
Private Secretary

Recycled Paper

SCANNED

DRAFT LETTER FOR THE PRIME MINISTER

Roger B Smith Esq
Chairman
General Motors Corporation
Detroit
Michigan 48202

I know that you were greatly disappointed by the Government's announcement of its intentions in relation to its Special Share in Jaguar.

I should like personally to reassure you that our decision was not in any sense intended to reflect a particular Government view on the future ownership of the company; ~~on which~~ we have been and remain entirely neutral on that issue. As ~~the Secretary of State for Trade and Industry, Mr~~ Nicholas Ridley, explained to Parliament on 31 October, however, the restrictions on shareholdings entrenched by the Special Share were causing uncertainties about the company's future by prompting speculation over how these powers would be exercised. ~~so~~ This in turn was distorting the basis on which all parties involved had to reach decisions. As the speculation intensified, we felt that the Government's position should be ~~clarified~~ made clear as a matter of urgency. It would have become invidious to have to make such a clarification as events developed.

Let me assure you ~~I wish there to be no misunderstanding~~ that the Government values very highly the contribution to the United Kingdom economy made by GM through its various operations in this country. I sincerely hope that we ~~and I am anxious that we should~~ continue to have a constructive dialogue with GM on ~~how these activities might be developed~~. the future development of these activities.

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the department for Enterprise

CONFIDENTIAL

1.20 pm

MARKET SENSITIVE

COMMERCIAL IN CONFIDENCE

JAGUAR: STATEMENT 1 NOVEMBER 1989

With permission Mr Speaker, I wish to make a statement on Jaguar plc.

Jaguar's Articles of Association contain clauses preventing any individual or concert party from holding an interest in more than 15 per cent of the company's shares. This is backed by the Government's Special Share which requires my written consent for changes in certain parts of the Articles until they lapse on 31 December 1990 when the Special Share itself is due to be redeemed. Any such change in the Articles would, besides my consent, also require the passing of a special resolution by shareholders in general meeting.

These provisions of the company's Articles were put into place to preserve Jaguar's independence in its formative years as a free-standing company and so allow its management to concentrate on developing the business without the constant distraction of unwelcome takeover bids. In recent months, however, I understand that the Chairman of Jaguar has been talking to a number of companies that are interested in forming links with Jaguar. There is a widespread perception that the company's financial and technological base needs strengthening in this way. The restrictions on shareholdings entrenched by the Government's Special Share are now clearly causing uncertainties about the company's future by prompting speculation over how my powers may be exercised, so distorting the basis on which all parties involved have to reach their decisions. I have accordingly today told the Jaguar management that, if shareholders pass a special resolution by the requisite 75% majority amending the ownership provisions of the Articles, then I shall be ready also to give my consent.

Recycled Paper

dti

the department for Enterprise

I am clear that it is in the best interests of Jaguar's management, shareholders and workforce for the company's future to be assured and the present climate of uncertainty resolved as quickly as possible. I have no doubt that the Jaguar board will continue to pursue their discussions with interested parties, and assess proposals, with the aim of recommending to the shareholders the solution that they believe to be in the interests of the company as a whole. This statement is intended to help towards this end and to pave the way for shareholders, with the advice of the Board to reach their own view on the options which may be available. The Government's role will henceforth be confined to consideration in the normal way of the competition policy aspects of any change in Jaguar's ownership.

CONFIDENTIAL

10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

31 October 1989

JAGUAR

The Prime Minister was grateful for your Secretary of State's minutes of 25 October and 30 October. The Prime Minister and your Secretary of State discussed the issues raised when they met this morning. It was agreed that your Secretary of State should make an announcement today indicating that the Government was waiving the golden share in Jaguar. This should, however, take the form of an Oral Statement to Parliament rather than a Written Answer.

I am sending copies of this letter to the Private Secretaries to the Lord President and the Chancellor of the Exchequer, and to Sir Robin Butler.

PAUL GRAY

Neil Thornton, Esq.,
Department of Trade and Industry.

CONFIDENTIAL

Jaguar PLC

Mr. Speaker: I call Mr. Ridley.

Mr. Joseph Ashton (Bassetlaw): On a point of order, Mr. Speaker.

Mr. Speaker: I will take points of order after the statement.

Mr. Ashton: It is on this matter, Mr. Speaker.

3.30 pm

The Secretary of State for Trade and Industry (Mr. Nicholas Ridley): With permission, Mr. Speaker, I wish to make a statement on Jaguar PLC.

Jaguar's articles of association contain clauses preventing any individual or concert party from holding an interest in more than 15 per cent. of the company's shares. This is backed by the Government's special share which requires my written consent for changes in certain parts of the articles until they lapse on 31 December 1990 when the special share itself is due to be redeemed. Any such change in the articles would, besides my consent, also require the passing of a special resolution by shareholders in general meeting.

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The restrictions on shareholdings entrenched by the Government's special share are now clearly causing uncertainties about the company's future by prompting speculation over how my powers may be exercised, so distorting the basis on which all parties involved have to reach their decisions. I have accordingly told the Jaguar management that, if shareholders pass a special resolution by the requisite 75 per cent. majority amending the ownership provisions of the articles, I shall be ready also to give my consent.

I am clear that it is in the best interests of Jaguar's management, shareholders and work force for the company's future to be assured and the present climate of uncertainty resolved as quickly as possible. I have no doubt that the Jaguar board will continue to pursue its discussions with interested parties, and assess proposals, with the aim of recommending to the shareholders the solution that it believes to be in the best interests of the company as a whole.

This statement paves the way for shareholders, with the advice of the board, to reach their own view on the options which may be available. The Government's role will henceforth be confined to consideration in the normal way of the competition policy aspects of any change in Jaguar's ownership.

Mr. Bryan Gould (Dagenham): I begin by welcoming the Secretary of State to the Dispatch Box and to his new responsibilities, but may I link that welcome with an expression of concern that, at his first appearance, he may well have lent himself to what looks suspiciously like a tactical device designed to delay the beginning of the important debate which is about to start? I commiserate with him that his first task is to announce the dispatch of yet another major British company—another victim of the Government's destructive policy towards manufacturing. His task is also to signal the disappearance of the last vestige of what had remained of the independent British car industry.

Does the Secretary of State agree that Jaguar remains and must remain a vital centre of engineering excellence of huge importance to the west midlands and that it is essential that it should remain a west midlands-based car manufacturing company with as much operational independence as possible?

Why, then, has the right hon. Gentleman so evidently abdicated his responsibilities in making this statement today? Who asked him to give up the golden share? What does it mean for other golden shares in other privatised companies? Is there now to be an open season on all golden shares? Does he not recognise that the end result of the market free-for-all which, in effect, he has announced will be that the Jaguar badge will be placed on cars designed and engineered elsewhere and that Jaguar will simply be swallowed up by one or other multinational with no guarantees or assurances whatsoever? Why did the Secretary of State not use his golden share to negotiate proper assurances from General Motors, Ford, Daimler or whomever else may be bidding while he still had a negotiating card in his hand? What is the point of putting a golden share into place if he dispenses with it as soon as it might serve a useful purpose?

Does the Secretary of State accept that his statement offers the clearest possible contrast between the irresponsibility of his Government and the proper concern that the next Labour Government will show for Britain's manufacturing base? Does he accept that his statement is a signal that, once again, market forces, for ideological reasons, will be allowed to deliver an important British enterprise to foreign predators? Does he further accept that the golden share is a charade, and that this is a black day for the west midlands and for the British car industry?

Mr. Ridley: I am surprised at the hon. Gentleman's opening remarks. He wrote to me on 20 September, stating:

> "If Jaguar do indeed need the financial and investment assistance to be obtained from becoming part of a larger group, does the Government have any other (and better) solution to offer? If not, may it not be better to help to bring the matter to a conclusion as soon as is reasonably possible, rather than insisting on prolonging the uncertainty until the expiry of the golden share?"

Even when I try to respond to the hon. Gentleman's request to bring the uncertainty to an end, he is grudging in his acceptance. The hon. Gentleman also seemed to say that he understands the need for a strong group to go into some form of partnership with Jaguar, which is what I said in my statement. All that I am doing now is to clear the way so that the playing field is level betweeen all contestants and so that there is no doubt or confusion about what the Government might do in the event of a takeover bid or of other proposals being put to the shareholders.

I agree that Jaguar has done remarkably well and that it is a vital centre of engineering in the west midlands. However, I believe that it will continue to do much better

The Prime Minister: Yes. As I said in reply to the first question this afternoon, under this Government wealth has been created and spread ever more widely. Under the last Labour Government, the Labour party took us to the IMF—bankrupt.

Mr. Healey: Does the Prime Minister agree with Lord Hailsham who said this weekend, speaking with all the authority of a former Lord Chancellor who had served for many years in the Prime Minister's Cabinet, that for the Prime Minister to use her press officers to undermine her colleagues was not only disloyal, but dishonourable? Will she now stop that?

The Prime Minister: This was a comment from my noble Friend. I was surprised at it and I was very surprised that he made it. It is totally untrue and in any case, I would never take it from the right hon. Member for Leeds, East (Mr. Healey), whose only adviser was the IMF.

Q5. **Mr. Andrew MacKay:** To ask the Prime Minister if she will list her official engagements for Tuesday 31 October.

The Prime Minister: I refer my hon. Friend to the reply that I gave some moments ago.

Mr. MacKay: Does my right hon. Friend agree that it would be a cruel deception to suggest that there is some painless way to bring down inflation and that if credit controls were introduced today, they would prove to be quite ineffective due to the international nature of the banking and financial markets?

The Prime Minister: I agree with my hon. Friend. The point was made effectively in the last debate on economic affairs when my right hon. Friend the Member for Worthing (Mr. Higgins) dealt very well with the issue of credit controls. They will not work in the modern world with a free and open banking system. In an earlier debate, a former Treasury Minister in a Labour Government said:

"The Labour Party idea that you can have credit controls is rubbish. There is no way you can control credit except by controlling the price of credit, and the price of credit is Bank Rate."

Mr. Nellist: To ask the Prime Minister if she will list her official engagements for Tuesday 31 October.

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Mr. Nellist: Is the Prime Minister aware that in a tragic car accident last week in Coventry, the firefighters cut the cars apart, the police directed the traffic and an ambulance worker was upside down for two hours in that car infusing blood to the victim? How then this morning can Duncan Nicholls say that the ambulance workers do not deserve parity with the other services? When will the Prime Minister stop chasing ambulances down to places like Clapham and King's Cross and praising ambulance workers and then treating them like dirt as she does now?

The Prime Minister: We all praise ambulance workers for their work and do not use them cheaply as the hon. Gentleman has done. Their pay claim, as the hon. Gentleman is aware, is being negotiated and I most earnestly hope that they will keep emergency cover until the negotiations are complete.

Q7. **Mr. Marland:** To ask the Prime Minister if she will list her official engagements for Tuesday 31 October.

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Mr. Marland: Is my right hon. Friend aware of the valuable contribution that is made to environmental protection by recycling—*[Interruption.]* Will she ensure that, under the forthcoming environmental protection Bill the work of the recycler is not interrupted by misleading definitions of waste?

The Prime Minister: Yes. Recycling, in all its forms, makes a great contribution to the economy, and we at No. 10 Downing street have introduced recycled paper.

Jaguar PLC

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The Prime Minister: Yes. Recycling, in all its forms, makes a great contribution to the economy, and we at No. 10 Downing street have introduced recycled paper.

Prime Minister

You did not have chance to look at the earlier paper over the weekend – I put them back in the first box this evening. Mr. Ridley now wants to bring the issue to a head – are you content for an immediate statement tomorrow waiving the golden share? ARC 30/10

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the department for Enterprise

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PRIME MINISTER

JAGUAR

I wrote to you about this on 25 October. In the light of recent and imminent developments, I think that we need to take an urgent decision on the golden share.

The Jaguar board are to meet at 10.30am this Wednesday (1 November). They are to consider progress in the negotiations with General Motors which, you will recall, would involve GM taking a minority stake in the company underpinning a major collaboration on car and engine development. They will also, however, have before them the proposition which Ford promised to table after their most recent discussions with Sir John Egan.

I have just been given an outline of the proposition and it is this which I believe requires us to act now. Ford intend to table an indication of readiness to make a full takeover bid, including a firm offer price per share together with an outline of the industrial and commercial package which they want to explore with Jaguar. If the board endorse the proposition - or, more likely, agree that it merits serious consideration - Ford envisage an immediate approach seeking my agreement to waiver of the golden share, so paving the way for a shareholder vote. Ford would hope for a rapid response from me.

If the board reject the proposition, Ford would have to reflect on their next move. Either way, however, news of their readiness to bid would quickly emerge. Under US law (the Williams Act),

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Ford will be required within 24 hours to file details of their intentions with the Securities and Exchange Commission. The document will then be in the public domain by Thursday afternoon at the latest.

I attach at Annex A a note which briefly outlines the substance of the respective Ford and GM offers. While GM are considering expanding production in Germany, Ford seem ready to do so in the UK. For what it is worth I therefore think that Ford's intentions would better preserve Jaguar as a British manufacturing operation and by the same token provoke less political difficulty.

But this is precisely the avenue of argument down which I see us being dragged by the golden share and from which I believe that we should try to escape by preemptive action. As I see it, once Ford's intentions are public, we shall clearly be pressed on our attitude to the golden share. If I say that we might be ready to waive it, that will be construed as a pro-Ford stance. If I indicate the reverse, we shall look to be backing GM. If I refuse to give a view, I shall just compound the existing commercial (and political) uncertainties.

In the options facing me, much would of course turn on the attitude of Sir John Egan and his board. But the worst scenario would be one under which the board rejected the Ford approach and Sir John sought my confirmation that the golden share would remain in place. I would then be left either to accept his request and so leave the shareholders unable to take a view; or to refuse it, so as to safeguard shareholder interests, and be accused of failing to defend the company from foreign predators.

I conclude from all this that it would be far better for us to make an immediate and clean break from the golden share by announcing tomorrow - before the Jaguar board meets - that, if

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75 per cent of shareholders vote to amend Jaguar's Articles so as to allow a full takeover by any party, then I shall be ready to give my consent. This statement will have to be non-discriminatory: I cannot indicate that waiver would be available for Ford or GM but not for any other suitor who might emerge.

I attach at Annex B a draft of the statement I would make. Subject to Geoffrey Howe's views, I envisage this as a written answer to an arranged Parliamentary Question. The Opposition will no doubt accuse me of abandoning Jaguar to a foreign predator, and dereliction of my duty in respect of the golden share. But I think we can argue convincingly in defence that Jaguar is in play as a takeover target; potential suitors want to strengthen the business rather than to close it down; continuing uncertainty is starting to damage the company; and it is better to provide a clear framework within which shareholders can consider the preferred future of the company without the distortion which the golden share introduces.

If you and colleagues agree with this approach, I shall tell Sir John Egan what we intend to do. If he voices strong objection on content or timing, I will come back to you.

I am copying this minute to Geoffrey Howe and John Major. I should welcome a very early indication of your and their views. I am also sending a copy to Sir Robin Butler.

N R

30 October 1989

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

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ANNEX A

JAGUAR: FORD AND GM INTENTIONS

FORD

1 They plan a full takeover bid, subject to waiver of the golden share and a shareholder vote, at a price per share which is not yet known.

2 The industrial and commercial package which they want to explore with Jaguar is said to involve:

(a) retention of manufacturing in Coventry, with significant expansion there or elsewhere in the UK, probably including construction of an extra plant;

(b) support for Jaguar to develop a new small car, positioned at or just below the BMW 5 series segment;

(c) investment totalling up to £1 billion for (a) and (b) together;

(d) retention of Jaguar's R and D facility at Whitley, strengthened through links with Ford's US and UK facilities;

(e) major benefits in component purchasing in terms of both price and quality;

(f) support for expansion of Jaguar's own marketing network in the USA, Europe and the Far East.

GENERAL MOTORS

3 Jaguar told us on 13 October that a deal with the following elements was in prospect:

(a) GM would take an immediate stake of 15 per cent in Jaguar (5 per cent through the issue of new shares and 10 per cent through a tender offer to existing shareholders), with the aim of increasing the total to 21 or 22 per cent in January 1991 through a new share issue;

(b) Jaguar would receive an immediate cash boost of some £180-200 million made available in part through a loan from GM repayable from the proceeds of the new share issue in 1991;

(c) joint development of a new Jaguar-badged car, below the existing model range, to be financed largely by GM, built at their Opel plant in Germany, and sold

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through a jointly-owned GM/Jaguar distribution network;

(d) joint development of a new engine for the car, perhaps as part of a larger engine project which GM are considering for Europe (manufacturing location unknown);

(e) the whole package to be subject to approval by a simple majority of Jaguar shareholders at an extraordinary general meeting.

4 On 16 October the Jaguar board decided that clauses in the collaborative car project, which would impose accelerating financial penalties on Jaguar in the event of termination, would be regarded by shareholders as a poison pill deterring others from bidding for the company when the golden share expired. Following renegotiation with GM, we understand that this difficulty has been more or less resolved. But we do not know the details, nor whether the Jaguar board will be satisfied.

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ANNEX B

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JAGUAR: ARRANGED PARLIAMENTARY QUESTION AND ANSWER

To ask the Secretary of State for Trade and Industry: whether he will make a statement on Jaguar plc.

Jaguar's Articles of Association contain clauses preventing any individual or concert party from holding an interest in more than 15 per cent of the company's shares. This is backed by the Government's Special Share which requires my written consent for changes in those parts of the Articles until they and the Special Share itself lapse on 31 December 1990. Any such change in the Articles would, besides my consent, also require the approval of a special resolution of the company by 75 per cent of shareholders who vote at an extraordinary general meeting.

The Special Share was put in place to preserve Jaguar's independence in its formative years as a free-standing company and so allow its management to concentrate on developing the business without the constant distraction of unwelcome takeover bids. In recent months, however, I understand that the Chairman of Jaguar has been talking to a number of companies that are interested in forming links with Jaguar. There is a widespread perception that the company's financial and technological base needs strengthening in this way. The restrictions on shareholdings entrenched by the Government's Special Share are by now clearly causing uncertainties about the company's future by prompting speculation over how my powers may be exercised, so distorting the basis on which all parties involved have to reach their decisions. I have accordingly today told the Jaguar management that, if 75 per cent of shareholders vote in favour of a special

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resolution amending the Articles so as to allow a full takeover by any party, then I shall be ready to give my consent.

I am clear that it is in the best interests of Jaguar's management, shareholders and workforce for the company's future to be assured and the present climate of uncertainty resolved as quickly as possible. This reply is intended to help towards this end and to pave the way for shareholders to reach their own view on the options which may be available. The Government's role will henceforth be confined to consideration in the normal way of the competition policy aspects of any change in Jaguar's ownership.

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30. 10. 1989

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PRIME MINISTER

FUTURE OWNERSHIP OF JAGUAR - SPECIAL SHARE

The attached minute from Nick Ridley sets out the provisional view that, with Jaguar now coming "into play", the Government should seriously consider waiving the Golden Share in advance of the December 1990 expiry date.

Thus far, the issue of the use of the Golden Share has not arisen; Ford and any other hostile bidders have not come forward with proposals for going above a 15 per cent shareholding. But I gather from the Department of Trade and Industry, since Mr Ridley sent his minute, that there is a possibility of a bid for the whole of Jaguar emerging next week. So the issue could soon become a live one.

You will want to consider whether you agree that it might be appropriate to waive the Golden Share ahead of time. I have discussed this with George Guise and others in the Policy Unit, and we all feel there is a strong case for waiving it:

- There was never anything magic about the period of five years. A period with a Golden Share was designed to give the company time to get through its formative years. Arguably, that has now occurred. And if the forces of the market are bringing the question of future ownership to a head now, so be it.

- There must be serious question marks over Jaguar's long-term viability as an independent. If some form of restructuring is needed why prevent this happening for a further year?

- Waiving the golden share returns the issue of the future of the company to where it genuinely belongs, ie with the shareholders. And there is no change to the articles possible, even after the Golden Share has gone, unless 75 per cent of those at an EGM vote for it.

b

Against that, you will want to consider the politics of allowing Jaguar to move now into foreign hands.

Content to support Mr Ridley's provisional views that serious consideration should be given to waiving the golden share now?

I doubt whether we need to. We could always agree to an offer if it was thought desirable for Jaguar. If we waive this one early - there can never be any confidence that it won't be another golden share

RLC6

PAUL GRAY
27 October 1989

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PRIME MINISTER

FUTURE OWNERSHIP OF JAGUAR

As you know, potential takeover speculation surrounding Jaguar has been intense in the last month. Matters may come to a head very shortly and we shall need to be ready to react quickly if circumstances demand.

I attach a note which sets out the background. Briefly, Ford and General Motors both want to bring Jaguar under their wing - Ford through a full takeover, and GM (so far at least) by a minority stake underpinning a major collaboration on car and engine development. On the positive side, they are motivated by Jaguar's cachet as a luxury car marque which would fill the gap at the top of their own rather prosaic executive model ranges. Negatively, they each seem determined to keep Jaguar out of the other's hands.

I am engaged for two reasons:

(i) through my competition policy responsibilities, where it will be for the Director-General of Fair Trading to advise me on whether the taking of a full or partial stake in Jaguar by either party merits an MMC reference; and

(ii) through my holding of the "golden share" in Jaguar which gives me power of approval over individual or concerted shareholdings above 15 per cent until 31 December 1990.

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The discharge of my responsibilities for the first aspect should, of itself, create no particular problem. The Director-General will proceed in the usual way and I shall need fully to consider his advice. Without prejudice to his views, I would not expect there to be difficulties of this sort in relation to the bids by either GM or Ford. I would also hope that, in both their cases, his advice could be with me by the time I have to take decisions on the golden share. Any counter-bidders who emerged subsequently would have to recognise that this would probably not be true for them: their bids would have to be subject to consideration of the competition aspects. I see no particular difficulty in this.

As regards the golden share itself, it by now seems very likely one way or another that I shall be asked to waive it so as to allow a full takeover of the company. The deal which Jaguar have been negotiating with GM would not as so far constructed, have raised the issue. But Ford now look set to mount a full bid, which would require a waiver; and, if they act in this way, I think that GM may feel bound to make a parallel counter-bid.

A US takeover of Jaguar, before expiry of the golden share, raises obvious political difficulties. Their extent would depend in part on whether a bid had the backing of the Jaguar board, and subsequently its shareholders, as well as on the perceived "Britishness" of the associated plans for development of the company. But the fact is that the company is now in play as a takeover target. And the golden share protection anyway expires in just over a year,s time. To block a takeover now would simply delay the inevitable and continue the uncertainty which Sir John Egan now believes to be damaging the company. All seem to be agreed that Jaguar does urgently need the support of a major car manufacturer, both for its financial and technological development.

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My provisional view is that we shall have to consider seriously a waiver of the golden share. This would open the way to a bid, but only if 75% of the shareholders who voted at an EGM supported the relevant change in the Articles. Once waived, other bidders - perhaps less welcome than Ford or GM - could step in. There are arguably few, if any, companies able and willing to take on Ford/GM, but I am considering the likelihood and implications of this. Daniela-Bez.

I am following events closely and will keep you informed of significant developments.

I am sending a copy of this minute to Nigel Lawson and to Sir Robin Butler.

N R

25 October 1989

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FUTURE OWNERSHIP OF JAGUAR

INTRODUCTION

1 This note:

(a) describes the background to and nature of the Government's golden share in Jaguar;

(b) reports the latest position in the swirl of potential takeover activity now surrounding the company.

THE GOLDEN SHARE

2 In 1982 the Government set British Leyland the objective of returning all its businesses, together or separately, to the private sector as soon as practicable. After the 1983 election, privatisation of Jaguar - the most saleable proposition in the BL portfolio - came to the top of the agenda.

3 In February 1984 E(A) decided against BL's proposal for partial flotation of Jaguar but with BL retaining a blocking minority stake of 25.1 per cent to guarantee its independence. Instead, Ministers agreed on a full flotation, though arranged so as to give the possibility of preventing control of the company passing abroad either immediately or in the foreseeable future.

4 The so-called "golden share" was the method chosen. It operates as follows. Jaguar's Articles of Association contain clauses preventing any individual or concert party from holding an interest in more than 15 per cent of the company's shares. This is backed by the Government's £1 Special Rights Redeemable Share which allows - but does not require - the Secretary of State to block changes in those parts of the Articles. In addition, the share prevents the company from disposing of any significant assets (accounting for more than 25 per cent of either net assets or profits) without his consent.

5 The restrictions in the Articles are to lapse when, as provided, the golden share is redeemed on 31 December 1990. Until then, any change in the relevant clauses would require both the Secretary of State's consent and a special resolution of the company backed by 75 per cent of the shareholders who choose to vote. Redemption of the golden share on the due date is automatic: any extension would require the same procedure.

6 Jaguar was duly floated on this basis in July 1984. The golden share attracted no real controversy. Then and since, the Government have justified it as a measure to guarantee

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Jaguar's independence in its formative years as a free-standing company and so allow its management to concentrate on developing the business without the constant distraction of unwelcome takeover bids whether from foreign or domestic sources.

7 Three other points are worth noting:

(a) largely for EC reasons, the Government have all along been careful not to single out foreign predators as the prime target of the golden share;

(b) there has never been any hint that the share might not be used to block a shareholding above the limit;

(c) on the other hand, there has never been any hint that it might be extended beyond 1990. On the contrary: all Government statements, and the Jaguar flotation documents, have made clear that it will lapse on the due date. Beyond that, since the Stock Exchange agreed with great reluctance to the arrangements in 1984, they could be expected to react strongly against any idea of extension.

CURRENT TAKEOVER ACTIVITY

8 Since privatisation, Jaguar has made great strides in profitability, quality, efficiency and productivity. But for three main reasons observers inside and outside the world car industry doubt whether Jaguar has a future as an independent company:

(a) with about 40 per cent of production exported to the USA, it is heavily exposed to exchange rate risks in a market so competitive that compensating price increases are often impossible (especially since the Japanese have just begun to enter the luxury car sector);

(b) Jaguar remains essentially a single-product company on a small scale. With output of 50,000 cars a year compared to (eg) BMW's 500,000, there are doubts whether it can generate the cash to support the extensive R and D necessary for a high tech producer and still less to allow expansion of its model range;

(c) product quality and labour relations, though improved, still suffer recurrent problems.

9 Despite these factors, the Jaguar marque retains great cachet. By now, most of the world's major car producers are

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known or rumoured to want to form some link with the company, ranging from full takeover to a partial stake which would underpin collaboration in areas such as model development, R and D and marketing. Jaguar management - who recognise the company's vulnerability - have been searching for a solution which would both retain the company's independence and stand a chance of being acceptable to shareholders.

10 Recently, BMW and Daimler-Benz have each told DTI Ministers of their interest in taking a minority stake in Jaguar to underpin collaboration of one sort or another. And Volvo have signalled their interest in an eventual full takeover. Those companies apart, market and press rumours have put a wide range of other suitors in the frame, including VW/Audi, Peugeot, Renault, Fiat, Chrysler, Toyota, Nissan and Mitsubishi. But the real action is now centred on Ford and GM, who seem increasingly determined to tie up with Jaguar as much to lock each other out as for its own merits as a company.

FORD

11 Ford told the Government on 19 September that, subject to the approval of US anti-trust regulators, they intended to buy up to 15 per cent of Jaguar shares in the market. Approval was granted on 6 October. By 16 October Ford confirmed that they had secured over 19 million shares representing just over 10 per cent of the total equity.

12 Ford originally said that their action marked their long-term interest in deepening collaboration with Jaguar, probably through extending their stake once the golden share lapsed. Their aim would be to see autonomy retained, and they would be able to strengthen Jaguar in R and D, marketing, scale economies in component purchasing and not least financial muscle. Sir John Egan and the Jaguar board at once described Ford's move as unwelcome, confirming that they would continue to look for a way of retaining independence. This has since taken the form of the intensive negotiations with GM which are described below and which in broad terms have emerged publicly.

13 On 16 October Ford reacted to the rebuff, and to GM's inside-track status, by telling Sir John Egan that, subject to approval by the US board, they were ready to bid for the whole company and, jointly with Jaguar, to seek the Government's approval for the lifting of the golden share restrictions. They agreed to present Jaguar with formal proposals, including the buy-out price and ideas for the company's future development, by Monday 30 October at the latest (and probably before then).

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14 Separately, Ford have given the Department an outline of their thinking. This is still provisional because, unlike GM, they have had no detailed discussions with Jaguar and so do not fully understand the company's present position and prospects. Subject to this caveat, they say that:

(a) they intend Jaguar to run as an "autonomous" part of the Ford business, with its manufacturing base continuing in the UK;

(b) volume, including new models, could be expanded two or three times (ie to 100,000-150,000 cars a year);

(c) there would be close collaboration in R and D, marketing, component purchase and model development.

GENERAL MOTORS

15 In his search for continued independence, Sir John Egan has long seen GM as his preferred suitor. Negotiations on a possible deal began in July and have continued behind the scenes until recently.

16 Ford's statement of intent on 19 September has since sharpened the pace significantly. On 13 October Jaguar told the Department that a deal with the following elements was in prospect:

(a) GM would take an immediate stake of 15 per cent in Jaguar (5 per cent through the issue of new shares and 10 per cent through a tender offer to existing shareholders), with the aim of increasing the total to 21 or 22 per cent in January 1991 through a new share issue;

(b) Jaguar would receive an immediate cash boost of some £180-200 million made available in part through a loan from GM repayable from the proceeds of the new share issue in 1991;

(c) joint development of a new Jaguar-badged car, below the existing model range, to be financed largely by GM, built at their Opel plant in Germany, and sold through a jointly-owned GM/Jaguar distribution network;

(d) joint development of a new engine for the car, perhaps as part of a larger engine project which GM are considering for Europe (manufacturing location unknown);

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(e) the whole package to be subject to approval by a simple majority of Jaguar shareholders at an extraordinary general meeting.

JAGUAR BOARD REACTION

17 At this stage the Ford and GM stories come together. On 16 October the Jaguar board considered the GM deal. They were worried that clauses in the collaborative car project, which would impose accelerating financial penalties on Jaguar in the event of termination, would be regarded by shareholders as a poison pill deterring others from bidding for the company when the golden share expired. They instructed Sir John Egan to reopen negotiations on this aspect with GM. Meanwhile, Ford have tabled their offer of full control and undertaken to submit detailed proposals by 30 October at the latest.

18 Sir John Egan has told us that he is conscious both of the need to get a deal which is in the best interests of shareholders but also of the damaging effects of prolonged publicity and uncertainty on the business. He aims to strike the best deal he can with either bidder. He thinks that it will be hard to decide between the merits of a partial bid from GM as against a full one from Ford, nor is he sure how far Jaguar can shelter behind the golden share if it wished to do so. He does not know if he will ask the Government to lift the golden share restrictions, though he may well do so. Although proposals have come from other companies, in his view none seem competitive with either Ford or GM.

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cc DTI

10 DOWNING STREET
LONDON SW1A 2AA

THE PRIME MINISTER

26 September 1989

Dear Mr. Lindsey Halstead,

Thank you for your letter of 19 September providing advance notice of your announcement on Jaguar.

I know that Mr Barron has already given the Secretary of State for Trade and Industry a more detailed account of Ford's interest in Jaguar and Mr Ridley has agreed it would be helpful if his Department could be kept in touch with significant developments in Ford's position.

Yours sincerely

Margaret Thatcher

L. Lindsey Halstead, Esq.

PRIME MINISTER

You signed over the weekend the attached letter to Mr Lindsey Halstead of Ford. This was drafted by DTI.

On reflection, I feel that the first paragraph is a bit too welcoming. I have now agreed the revised version below with DTI.

Content to sign the new version? (I think it would be better just to sign 'Dear Mr Halstead' and to omit the 'Lindsey'.)

PLG.

PAUL GRAY
25 September 1989

10 DOWNING STREET

LONDON SW1A 2AA

THE PRIME MINISTER

Dear Mr. Lindsey Halstead.

Thank you very much for your letter of 19 September. It was very helpful to have had advance notice of your announcement on Jaguar.

I know that Mr. Barron has already given the Secretary of State for Trade and Industry a more detailed account of Ford's interest in Jaguar and Mr. Ridley has agreed it would be helpful if his Department could be kept in touch with significant developments in Ford's position.

Yours sincerely

Margaret Thatcher

L. Lindsey Halstead, Esq.

dti

the department for Enterprise

COMMERCIAL IN CONFIDENCE AND MARKET SENSITIVE

The Rt. Hon. Nicholas Ridley MP
Secretary of State for Trade and Industry

. Paul Gray Esq
Private Secretary to the
Prime Minister
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Our ref PB5ABK
Your ref
Date 22 September 1989

Dear Paul, top enc

Thank you for your letter of 20 September. I should be grateful if this letter could be shown only to those with a need to see it.

The Prime Minister should be aware of other recent developments on Jaguar. Sir John Egan has alerted us to discussions in train with another motor manufacturer "of equal standing" to Ford which, if successfully concluded, might lead to the announcement of a deal within the next couple of weeks. This could take the form of a minority shareholding, based on the issue of new shares, initially within the 15% allowed by the Articles of Association but perhaps rising later, when the Articles permit, to a 25% stake. It would require the approval of shareholders.

The shareholding would underpin a major collaboration with the prospective partner involving the supply of components; collaboration on the development of a new, smaller car (the manufacturing location of which is not yet clear); and access to R&D, financial and marketing muscle. Under these arrangements, no approval would be required under the Government's "golden share".

Sir John was reluctant to disclose the name of the negotiating partner but we believe this to be General Motors who advised Lord Young in July that a deal on the above lines was under discussion with Jaguar (though GM at that stage did not want us to disclosure our knowledge of this to Sir John Egan). The GM presentation included the possibility of a linkage between Jaguar and Group Lotus, which GM already own, in structuring the new arrangements.

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Sir John has sought no endorsement of his plans from my Secretary of State; but he did express the hope that he would feel able to take no position as between competing interests. Mr Ridley simply noted that a response would only be appropriate from him if either party sought to change the Articles while the golden share remained in place (which Sir John said his proposals would not); or if proposals were made which brought into play his powers under the Fair Trading Act. Since neither had yet happened, he had no comment to make.

We have each in the last 24 hours also had approaches from Barings on behalf of Daimler-Benz. Other parties, including Volvo who have in the last few days declared to us their interest in Jaguar, may surface in due course. I will keep you informed on significant developments.

Letter for signature in the folder. PRCG

I attach a short, draft acknowledgement to Mr Halstead's letter of 19 September to the Prime Minister.

Yours ever,

Neil Thornton

NEIL THORNTON
Private Secretary

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COMMERCIAL IN CONFIDENCE AND MARKET SENSITIVE

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Our ref PB5ABK
Your ref
Date 22 September 1989

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COMMERCIAL IN CONFIDENCE AND MARKET SENSITIVE

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Yours ever,

Neil Thornton

NEIL THORNTON
Private Secretary

the Enterprise initiative

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SECRET

Note 1/a-6

1. Rang Barings and told them PM did not wish to see Leiner.
2. Reported above to Neil Thornton c DTI.

PREM 2/5

PRIME MINISTER

JAGUAR

I attach a note from Mr Ridley's office which summarises contacts between the DTI, Jaguar and other interested parties.

You should also be aware that there have been various related - though in some ways rather different -contacts between interested parties and No.10.

First, George Guise was contacted by Schroders, who claimed to be acting on behalf of General Motors and John Egan. They said they were considering putting together an alternative package involving GM taking an initial 15 per cent shareholding in Jaguar, to be followed once the golden share had lapsed by a move to, say, 29.9 per cent - i.e. below the Takeover Panel threshold requiring a full bid. The implication seemed to be that Egan would remain in charge - and Egan is said to be strongly in favour of this approach rather than the Ford move.

But the main message Schroders wished to pass on was that Egan had assured them he had been given a clear indication that you would be interested in receiving full details of this alternative approach; and indeed if this material could be got to No.10 by mid-day today (Friday) it could be faxed out to you in Moscow. After doing various bits of checking, I asked George Guise to go back to Schroders saying there was nothing in this story; if Schroders wanted to send No.10 any material this would simply receive a polite acknowledgement and be passed on to the DTI. George discreetly pressed for more information on where Egan had got his idea from, and eventually the name Alan Curtiss was mentioned.

Second, I have today been rung by Barings. They had been asked by Dr Gerhard Leiner of Damlier Benz to pass on a request to meet you next week to discuss Jaguar. Leiner had said he had a long conversation with you over lunch in Austria on 17 August, and he was sure that you would want to continue the conversation in the light of latest developments. I said that I would naturally pass

SECRET

6

on the request for a meeting to you; but my clear expectation was that you would not consider a further meeting was appropriate. Whatever informal conversation you may have had in Austria when the future of Jaguar was largely theoretical, we were now in a totally new position and I did not think you would consider it was appropriate to meet any of the players or potential players in Jaguar's future.

DTI would I believe strongly agree with my firm view that you should avoid any contacts of this sort at this stage.

Content that I should turn down the request for a meeting from Leiner and discourage any other interested parties from thinking there is any point in sending you material about Jaguar or requesting a meeting?

Yes
not

- Leiner mentioned his interest to me in Austria. I merely took note.

- I picked up other rumours and noted them but understood that hard info. would go to DTI.

I merely want to know the facts, not to influence events - that is NOT for me.

RRCG.

Paul Gray
22 September 1989

c:Jag (MJ)

10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

20 September 1989

FORD INTEREST IN JAGUAR

Thank you for your letter of 19 September enclosing the copy of your letter your Secretary of State received yesterday from Mr Lindsay Halstead and also attaching the line your Press Office would be using.

I now attach the letter the Prime Minister was sent by Mr Halstead which, as you will see, was in virtually identical terms. I shall be grateful if you could let me have an appropriate short reply for the Prime Minister's signature. It would be helpful to have this by Friday 22 September.

Paul Gray

Neil Thornton Esq
Department of Trade and Industry.

dti

the department for Enterprise

The Rt. Hon. Nicholas Ridley MP
Secretary of State for Trade and Industry

Paul Gray
PS/Prime Minister
10 Downing Street
LONDON SW1

Department of Trade and Industry

1-19 Victoria Street
London SW1H 0ET

Enquiries
01-215 5000

Telex 8811074/5 DTHQ G
Fax 01-222 2629

Direct line 215 5623
Our ref PE2ABY
Your ref
Date 19 September 1989

Dear Paul, he didn't

FORD INTEREST IN JAGUAR

I enclose a copy of the letter my Secretary of State received this afternoon from Mr Lindsay Halstead, Chairman of Ford of Europe, about his company's intentions towards Jaguar. I understand the Prime Minister received a similar letter.

Mr Halstead indicates that Ford are seeking clearance under US law to take up to a 15% holding in Jaguar, and hints that this may lead to a full bid at a later stage. He comments on the level of world competition in the luxury car market with the implication that Jaguar will find it very tough indeed to go it alone.

Mr Halstead's letters can be regarded as a courtesy only, and require no response from Government. Ford's proposals are within the terms of Jaguar's Articles of Association; the question of use of the Government's "golden share" does not arise.

I attach a copy of the line, approved by my Secretary of State, which DTI Press Office will be using with enquiries. Mr Ridley does not think it appropriate to take up Mr Halstead's offer of a meeting - and would not recommend the Prime Minister to do so - since he believes this would be incompatible with the Government's position on Ford's proposals. DTI officials will however keep in informal touch with Ford.

Yours ever.
Neil Thornton

NEIL THORNTON
Private Secretary

Recycled Paper

Annex

FORD INTEREST IN JAGUAR

LINE TO TAKE

- Ford are operating within the terms of Jaguar's Articles of Association. No approval was required of Government and none was sought

- as a courtesy, Ford notified Government in advance of their intentions

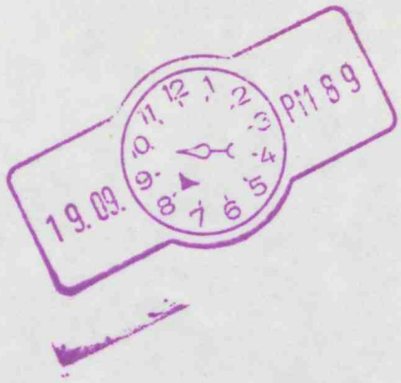
- the future of Jaguar after the expiry of the Government's special share in December 1990 will be a matter for the company and its shareholders.

DEFENSIVE

- The question of using the special share does not arise

- Government reaction to any proposals which brought the special share into play is entirely hypotehical.

PE2ABY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R, 19/9

Ford of Europe Incorporated
Chairman of the Board

Brentwood Essex CM13 3BW
England

September 19, 1989

Dear Prime Minister,

I am writing to you in the context of an important announcement, that we are making today. This concerns our desire to increase Ford's participation in the prestige sector of the world's car markets.

We have advised Sir John Egan today that Ford intends to make a filing with the U.S. authorities which would enable it to acquire a shareholding of up to 15 percent in Jaguar (the maximum shareholding permitted under Jaguar's Articles of Association until the end of 1990).

We believe that there would be substantial benefits in a long term association between Ford and Jaguar and we would seek to build on Jaguar's heritage as a manufacturer of fine sports and luxury cars.

If our stake in Jaguar were to increase at some time in the future, we would expect to maintain it as a separate and autonomous entity and reinforce its image as a manufacturer of exclusive and prestige cars. We would strengthen the company by providing access to the full range of Ford's financial and technological resources, and by enabling it to draw on our extensive capabilities in European, American and other world markets.

Cont'd...

The outlook for the prestige car markets, in Europe, North America and Asia, is one of increasing competitive pressures. In addition to the traditional German competitors, all the major Japanese manufacturers, for example, are introducing new product ranges which will compete directly with Jaguar. In this environment, the smaller companies will find it increasingly difficult to survive and prosper. We believe that an association between Jaguar and Ford is the best way to make Jaguar a stronger competitor in world markets and that such an association would therefore, be in the best interests of the company, its employees and shareholders.

We are also advising the Secretary of State for Trade and Industry, Mr Nicholas Ridley, of our intentions. I would of course be very pleased to meet with you to explain our plans in more detail if you wish.

With my best personal regards,

L Lindsey Halstead

The Rt. Hon. Margaret Thatcher, MP
The Prime Minister
10 Downing Street
London SW1
England.

RA

Ford of Europe Incorporated

Murray L. Reichenstein
Vice President - Finance

Brentwood Essex CM13 3BW
England

September 19, 1989

Professor Brian Griffiths
Prime Minister's Policy Unit
10 Downing Street
London
SW1A 4AA

Dear Professor Griffiths:

I thought you would want to know a little more about the background to the announcement we are making today about our decision to seek a minority shareholding in Jaguar plc.

The outlook for the prestige car markets, both in Europe and North America, is one of increasing competitive pressures. All the major Japanese manufacturers, for example, are planning to introduce new up-market brands which will compete directly with Jaguar and the already strong German companies. In this environment, the smaller companies will find it increasingly difficult to survive and prosper. An association between Jaguar and Ford could make Jaguar a stronger competitor in world markets, and would therefore be in the best interests of the company, its employees and shareholders and the British motor industry.

/....

Incorporated with Limited Liability in the State of Delaware, U.S.A.

Should our stake in Jaguar grow at some time in the future (the maximum shareholding permitted under Jaguar's articles until the end of 1990 is 15 percent), it would be our intention to maintain it as a separate and autonomous entity and reinforce its image as a manufacturer of exclusive and high quality cars. In the longer term, the benefits to Jaguar would include:

- Ford's considerable financial strength;
- Ford's experience of operating for 21 years as the most "European" of all the major car companies -- of particular benefit with regard to "1992";
- Ford's experience and strength in the United States -- Jaguar's most important market;
- cost savings on purchased materials and components because of Ford's much greater volume of purchases;
- and, most important, access to the full range of Ford's advanced technologies and research (as you may be aware, these include considerable in-house expertise in electronics).

I would be very pleased to meet with you and to explain our position in more detail if you should so wish.

Yours sincerely,

Jacques Reichenstein

MR. POWELL

PROPOSED FORD SHAREHOLDING IN JAGUAR

The Prime Minister will want to be aware of the attached letter from the Chairman of Ford of Europe. He reports that Ford are planning to take a shareholding of up to 15 per cent in Jaguar. An announcement is promised for today, although so far none has materialised (17.30 our time).

Under the terms of the special share there is nothing under UK law or business practice to stop Ford, or anyone else, taking a shareholding of up to 15 per cent; the special share arrangements only come into operation above that level. But it seems a fair bet that Ford are positioning themselves to be able to add to their shareholding when the special share expires at the end of 1990.

The reference to "filing with the US authorities" reflects the US requirement for US-owned companies to seek authority to acquire shareholdings in excess of 2 per cent. We have no parallel requirement in this country.

Now that Ford have declared their hand it is likely that other predators may come into the open. And of course that may include some Japanese companies. As I understand it any other company that was listed in the United States would have to go through the same hoops as Ford; but companies without a US listing would be able to move straight away in the market to acquire up to 15 per cent of the shares.

I also attach a press line that the Department of Trade and Industry and No. 10 are taking, which you will want to pass on to Bernard.

PAUL GRAY
18 SEPTEMBER 1989

MRMCDP.FAX

R. 19/9

Ford of Europe Incorporated
Chairman of the Board

Brentwood Essex CM13 3BW
England

September 19, 1989

Dear Prime Minister,

I am writing to you in the context of an important announcement, that we are making today. This concerns our desire to increase Ford's participation in the prestige sector of the world's car markets.

We have advised Sir John Egan today that Ford intends to make a filing with the U.S. authorities which would enable it to acquire a shareholding of up to 15 percent in Jaguar (the maximum shareholding permitted under Jaguar's Articles of Association until the end of 1990).

We believe that there would be substantial benefits in a long term association between Ford and Jaguar and we would seek to build on Jaguar's heritage as a manufacturer of fine sports and luxury cars.

If our stake in Jaguar were to increase at some time in the future, we would expect to maintain it as a separate and autonomous entity and reinforce its image as a manufacturer of exclusive and prestige cars. We would strengthen the company by providing access to the full range of Ford's financial and technological resources, and by enabling it to draw on our extensive capabilities in European, American and other world markets.

Cont'd...

Incorporated with Limited Liability in the State of Delaware, U.S.A.

The outlook for the prestige car markets, in Europe, North America and Asia, is one of increasing competitive pressures. In addition to the traditional German competitors, all the major Japanese manufacturers, for example, are introducing new product ranges which will compete directly with Jaguar. In this environment, the smaller companies will find it increasingly difficult to survive and prosper. We believe that an association between Jaguar and Ford is the best way to make Jaguar a stronger competitor in world markets and that such an association would therefore, be in the best interests of the company, its employees and shareholders.

We are also advising the Secretary of State for Trade and Industry, Mr Nicholas Ridley, of our intentions. I would of course be very pleased to meet with you to explain our plans in more detail if you wish.

With my best personal regards,

L Lindsey Halstead

The Rt. Hon. Margaret Thatcher, MP
The Prime Minister
10 Downing Street
London SW1
England.

Annex

FORD INTEREST IN JAGUAR

LINE TO TAKE

- Ford are operating within the [illegible] of Association. No agreement [illegible] Government and none was sought

- as a courtesy, Ford notified [illegible] their intentions

- the future of Jaguar after the expiry of the Government's special share in December 1990 will be a matter for the company and its shareholders

DEFENSIVE

- The question of using the special share

- Government reaction to any [illegible] special share will play [illegible]

PE2ABY

Annex

FORD INTEREST IN JAGUAR

LINE TO TAKE

- Ford are operating within the terms of Jaguar's Articles of Association. No approval was required of Government and none was sought

- as a courtesy, Ford notified Government in advance of their intentions

- the future of Jaguar after the expiry of the Government's special share in December 1990 will be a matter for the company and its shareholders.

DEFENSIVE

- The question of using the special share does not arise

- Government reaction to any proposals which brought the special share into play is entirely hypotehical.

PE2ABY



ROVER GROUP

facts & figures 1989

ROVER GROUP

ROVER GROUP

LONDON
The Rover Group plc, 7-10 Hobart Place, London SW1W 0HH
Telephone: 01-235 4311

COVENTRY
Fletchamstead Highway, Coventry CV4 9DB
Telephone: 0203 75511

COMPANY STRUCTURE

The Rover Group *is Britain's largest motor manufacturer producing over half a million vehicles a year. The Group designs, manufactures and markets cars in the small, medium and executive size sectors; car-derived vans and specialist four-wheel drive vehicles.*

The Group became a wholly-owned subsidiary of British Aerospace in August 1988 when HM Government sold its majority shareholding to BAe.

As a consequence Rover Group is now part of Britain's largest manufacturing and engineering organisation and one of Europe's largest companies with a combined annual turnover of £7,500 million of which exports account for £5,000 million.

The Rover Group *with an annual turnover of £3,200 million and exports of over £900 million, is BAe's largest single business.*

MANAGEMENT

The Group has a single management structure covering all its business activities, with separate commercial divisions for its cars and specialist four-wheel-drive products.
The Chairman is Sir Graham Day.
The Managing Director is George Simpson.

ROVER GROUP AND THE UK ECONOMY

Largest manufacturer and biggest exporter

The Rover Group is the UK motor industry's largest manufacturer and biggest exporter, producing four out of every ten cars built in Britain and exporting nearly seven out of ten of all British car exports.

1988 PRODUCTION

Total UK car production	*1,227,310 units*
Rover Group car production (including Range Rover)	*497,771 units*

THE ROVER GROUP PRODUCES 41% OF ALL CARS BUILT IN BRITAIN



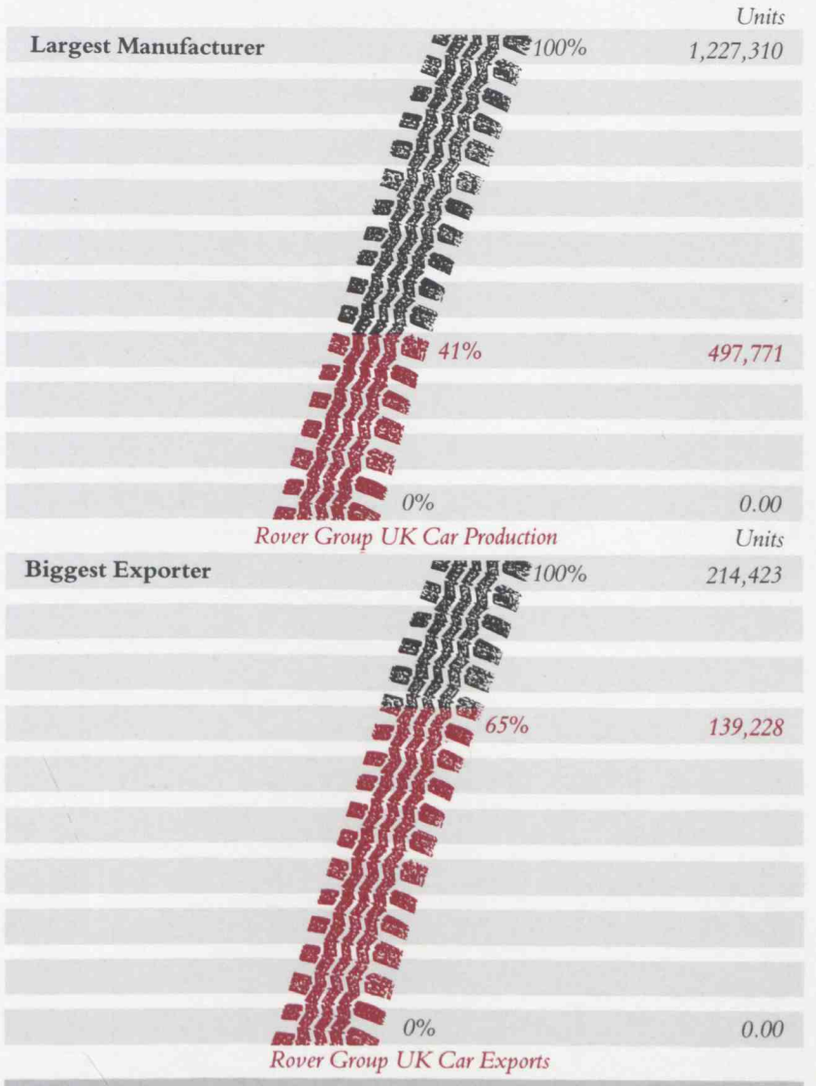
1988 EXPORTS

Total UK car exports	*214,423 units*
Rover Group car exports (including Range Rover)	*139,228 units*

THE ROVER GROUP EXPORTS 65% OF ALL CARS EXPORTED FROM BRITAIN



ROVER GROUP AND THE UK ECONOMY



ROVER GROUP AND EMPLOYMENT

Direct Employment

The Rover Group directly employs 41,700 people, of whom 40,500 are employed in Britain.

Indirect Employment

In the MANUFACTURING and SUPPLY SECTORS for every Rover Group job there are approximately three directly dependent jobs, mainly in the UK vehicle component manufacturing industry, amounting to 121,500 people.
In the RETAIL SECTOR, the 1,000 strong Rover Group UK dealer network employs 31,000 people.

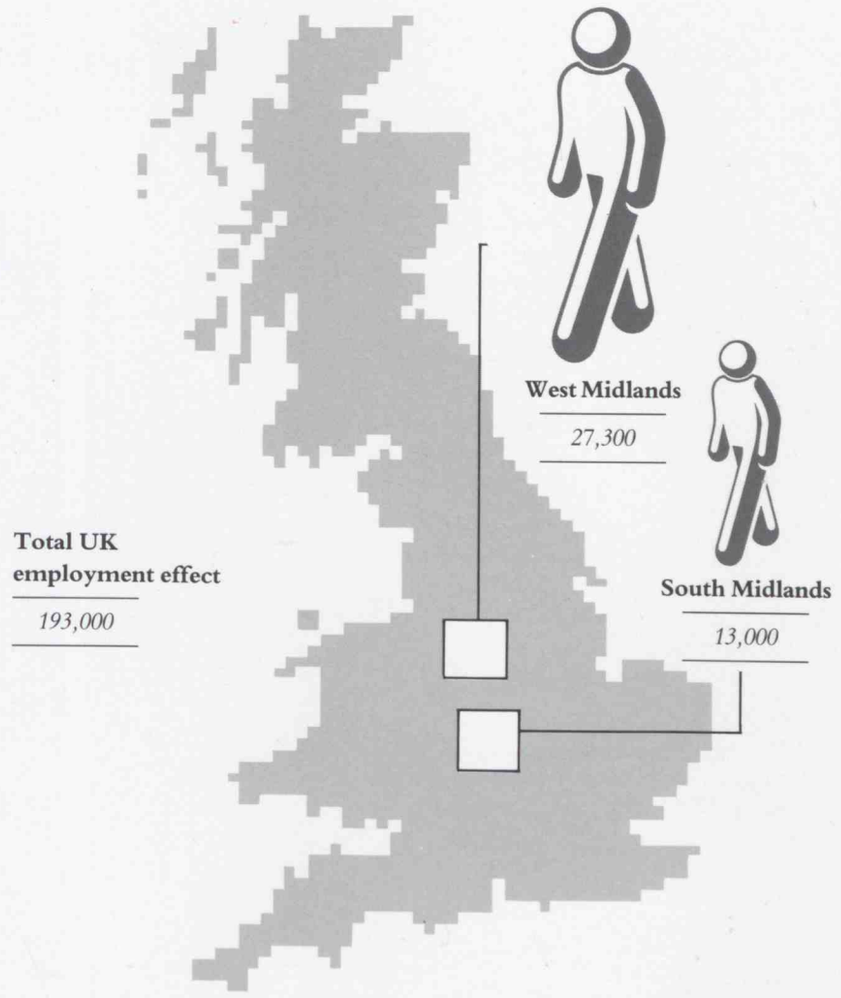
TOTAL UK EMPLOYMENT EFFECT

Rover Group	*40,500*
Dependent manufacturing and supply sectors	*121,500*
Dependent Retail Sectors	*31,000*
Total Employment Effect	*193,000*

The major areas of Rover Group employment are:

West Midlands		*27,300*
Birmingham	*15,900*	
Solihull	*8,900*	
Coventry	*2,000*	
Gaydon	*500*	
South Midlands		*13,000*
Oxford	*10,000*	
Swindon	*3,000*	

Rover Group UK Direct Employment *40,500*



Rover Group UK Indirect Employment *152,500*

MINORITY INTERESTS

The Rover Group has minority shareholdings in the following businesses which have either related or direct commercial links with the company.

COMPANY	ROVER GROUP SHAREHOLDING
DAF BV *A new commercial vehicle grouping formed by the merger of Leyland Vehicles and Freight Rover and the Dutch manufacturer DAF: The UK subsidiary company is Leyland DAF.*	*40%*
Istel Holdings Ltd *One of Europe's foremost information technology companies which provides systems and data services to Rover Group companies.*	*24.6%*
Llanelli Radiators Holdings Ltd *A major supplier to the UK motor industry, including Rover Group, of radiators, heat exchange equipment and seat frames.*	*25%*
UGC Ltd *The Unipart all-makes replacement parts and distribution company which provides a parts distribution service to Austin Rover.*	*21.7%*
JRA Holdings Ltd *Formerly Rover Group's Australian subsidiary, JRA distributes Austin Rover, Land Rover and other vehicle manufacturers products.*	*20.1%*

1988 ROVER GROUP PERFORMANCES STATISTICS

	AUSTIN ROVER	LAND ROVER	TOTAL ROVER GROUP	
Sales Revenue	*2,740*	*639*	*3,224**	*£ million*
Export Revenue	*508*	*400*	*908*	*£ million*
Sales	*493,400*	*46,700*	*525,000**	*units*
Production	*473,700*	*46,300*	*520,000*	*units*

*consolidated figures.

ANNUAL IMPACT ON UK ECONOMY	£ MILLION	
Purchase of production materials, goods and services	*2,000*	
Export earnings	*908*	
Value Added Tax (VAT) generated	*524*	
Car tax paid to government	*192*	
Employees disposable income	*434*	
Income tax paid by employees	*84*	
National insurance contributions by Rover Group and employees	*61*	
Cost of utilities (gas, water, electricity)	*35*	
Property rates	*19*	
TOTAL ECONOMIC EFFECT	*4,257*	*£ million*

AUSTIN ROVER

AUSTIN ROVER

Austin Rover markets cars and car-derived vans in the small, medium and executive sectors for sale in the UK and 50 overseas countries.



Rover 800 Saloon
Launched July 1986.
Eight model range of 2.0 and 2.7 litre executive cars.



Rover 800 Fastback
Launched May 1988.
Seven model range of 2.0 and 2.7 litre executive cars.



Sterling 800
Sedan launched January 1987.
5 door launched February 1989.
Three models of 2.7 litre, 4 and 5-door executive cars specifically for US market.



Rover 200
Rover 213 launched June 1984. Rover 216 launched March 1985.
Six model range of highly specified medium sized saloons with 1.3 and 1.6 litre engines.



Montego
Launched April 1984. MG Montego launched April 1985.
Eleven model range of 1.6 and 2.0 litre engine capacity.
Estates launched October 1984. Nine model range.
Diesel variants of both saloon and estate launched October 1988.

AUSTIN ROVER



Maestro
Launched March 1983.
Eight model range of 1.3, 1.6 and 2.0 litre engine capacity in medium hatchback market sector.



Metro
Launched October 1980 (3 door derivatives).
Launched October 1984 (5 door derivatives).
Fifteen model range with 1.0 and 1.3 litre engines.
One millionth Metro built on 21 October 1986.



Mini
Launched August 1959.
Two models of the car which pioneered small car family motoring, with transverse engine.
5 millionth Mini built in February 1986.

VANS



Metro
Launched 1982. Four model range, 1.0 and 1.3 litre engine capacity.



Maestro
Launched October 1984.
Eight model range with 1.3 petrol and 2.0 diesel engines.

LAND ROVER

Land Rover markets specialist four-wheel drive vehicles at home and overseas. Land Rovers and Range Rovers are sold in 150 markets throughout the world. Range Rover of North America is a wholly-owned subsidiary responsible for marketing the Range Rover in the United States.

MODELS

Land Rover

Launched 1948. 1 millionth Land Rover produced 1976. To date approximately 1.6 million vehicles have been produced.



Land Rover Ninety

(short wheel base) launched 1984.



Land Rover One Ten

(long wheel base) launched 1983.

Basic configurations: soft top, pick-up, hard top, station wagon, with 30 different versions.

Engines
2.5 litre petrol
2.5 litre diesel
2.5 litre diesel turbo
3.5 litre petrol



Range Rover

Launched 1970 (2-door)
Launched 1981 (4-door)

Engines
3.5 litre petrol
2.4 litre turbo diesel






OVERSEAS ASSEMBLY

Land Rover products are assembled overseas in the following countries:

AUSTRALIA
J.R.A. Ltd, Liverpool, New South Wales

KENYA
Leyland (Kenya) Ltd, Thika, near Nairobi



MALAYSIA
Land Rover (Malaysia), Selangor



TURKEY
Otobus Karoseri Sanayii A.S., Istanbul

ZAIRE
Inzal, Kinshasa

ZAMBIA
Rover Zambia Ltd, Ndola

ZIMBABWE
Leyland Zimbabwe Ltd, Harare



Overseas production is based on variants of the Land Rover One Ten long wheelbase vehicle.
Land Rover Ninety short wheelbase models are assembled in Malaysia in addition to One Ten vehicles.



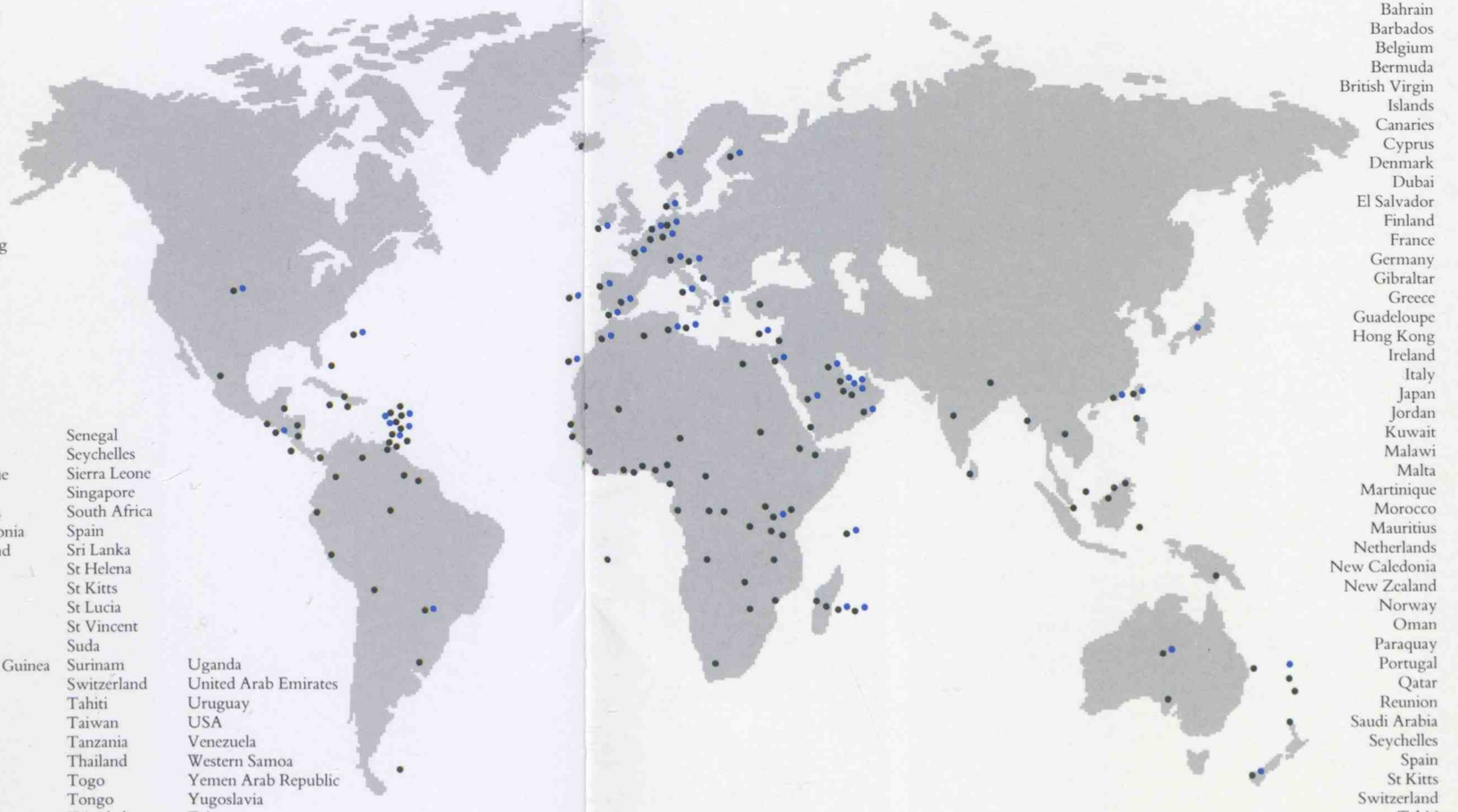





GEOGRAPHIC SPREAD OF WORLD MARKETS

LAND ROVER

Angola
Antigua
Algeria
Australia
Austria
Azores
Bahamas
Bahrain
Bangladesh
Barbados
Belgium
Belize
Benin
Bermuda
Bolivia
British Virgin Islands
Brunei
Burma
Burundi
Cameroon
Canary Isles
Central African Republic
Colombia
Congo
Costa Rica
Cote D'Ivoire
Cyprus
Denmark
Djibouti
Dominica
Dominican Republic
Ecuador
Egypt
Eire
El Salvador
Ethiopia
Falkland Islands
Fiji
Finland
France
French Guiana
Gabon
Gambia
Germany
Ghana
Gibraltar
Greece
Grenada
Guadeloupe
Guatemala
Guinea-Conakry
Guyana
Haiti
Honduras
Hong Kong
Iceland
India
Indonesia
Italy
Jamaica
Jordan
Kenya
Kiribati
Kuwait
Lebanon
Liberia
Luxembourg
Madagascar
Malagasy
Malawi
Malaysia
Mali
Malta
Mauritania
Mauritius
Mexico
Montserrat
Morocco
Mozambique
Nepal
Netherlands
New Caledonia
New Zealand
Nicaragua
Niger
Nigeria
Norway
Oman
Papua New Guinea
Panama
Paraguay
Peru
Philippines
Portugal
Qatar
Reunion
Rwanda
Sabah
Sarawak
Saudi Arabia
Senegal
Seychelles
Sierra Leone
Singapore
South Africa
Spain
Sri Lanka
St Helena
St Kitts
St Lucia
St Vincent
Suda
Surinam
Switzerland
Tahiti
Taiwan
Tanzania
Thailand
Togo
Tongo
Trinidad
Tunisia
Turkey
Tuvalu Islands
Uganda
United Arab Emirates
Uruguay
USA
Venezuela
Western Samoa
Yemen Arab Republic
Yugoslavia
Zaire
Zanzibar
Zambia
Zimbabwe



AUSTIN ROVER

Abu Dhabi
Australia
Austria
Azores
Bahrain
Barbados
Belgium
Bermuda
British Virgin Islands
Canaries
Cyprus
Denmark
Dubai
El Salvador
Finland
France
Germany
Gibraltar
Greece
Guadeloupe
Hong Kong
Ireland
Italy
Japan
Jordan
Kuwait
Malawi
Malta
Martinique
Morocco
Mauritius
Netherlands
New Caledonia
New Zealand
Norway
Oman
Paraquay
Portugal
Qatar
Reunion
Saudi Arabia
Seychelles
Spain
St Kitts
Switzerland
Tahiti
Taiwan
Tunisia
USA






OVERSEAS OPERATIONS

Austin Rover has national sales companies in the following markets:

BELGIUM
Austin Rover Belgium SA

GERMANY
Austin Rover Deutschland GmbH, also market Land Rover and Range Rover



SPAIN
Austin Rover Espana, also market Range Rover



FRANCE
Austin Rover France SA, also market Land Rover and Range Rover

IRELAND
Austin Rover Ireland Ltd, also market Land Rover

ITALY
Austin Rover Italia, also market Land Rover and Range Rover

JAPAN
Austin Rover Japan, also market Peugeot

NETHERLANDS
Austin Rover Netherlands BV, also market Land Rover and Range Rover




PORTUGAL
Austin Rover Portugal

UNITED STATES
Sterling Motor Cars






PURCHASE

Rover Group spends approximately £2,000 million each year with 2,100 suppliers, of whom 950 supply production materials. The Company's top twenty suppliers are:

BRITISH STEEL CORPORATION	*SOUTH WALES*
LUCAS GROUP	*BIRMINGHAM, NEWCASTLE-UNDER-LYME, WALES, BURNLEY*
GKN GROUP	*BIRMINGHAM, ROCHESTER, TELFORD*
BRUHL	*BIRMINGHAM, LEEDS*
AUTOMOTIVE PRODUCTS	*LEAMINGTON SPA*
DUNLOP GROUP	*COVENTRY, LEICESTER, MANCHESTER*
OXFORD AUTOMOTIVE COMPONENTS	*OXFORD*
VOLEX	*MANCHESTER*
DELANAIR	*SOUTH WALES*
TRW	*SOUTH WALES, BIRMINGHAM*
MARLEYFOAM	*KENT*
ZF GETRIEBE	*WEST GERMANY*
TUDOR WEBASTO	*BIRMINGHAM*
FIRTH FURNISHINGS	*HECKMONDWIKE*
PRESTAR	*BEDFORD, LUTON*
UNITED ENGINEERING & FORGING	*BIRMINGHAM*
HOBOURN GROUP	*ROCHESTER, BIRMINGHAM*
LLANELLI RADIATORS	*SOUTH WALES*
MAGNETTI MARELLI	*BIRMINGHAM*
MICHELIN	*STOKE-ON-TRENT, FRANCE*

ROVER GROUP FACTORIES

Rover Group employs 40,500 people at the following main factories and locations:

WEST MIDLANDS

Longbridge
Products: assembly of Rover 200, Metro, Mini, Honda Ballade. Engine manufacture, transmissions, castings.

Solihull
Products: assembly of Land Rover, Range Rover, engine and component manufacture, commercial and external affairs departments.

Drews Lane
Products: suspension units, engine components, axle and wheel assembly, brakes, steering systems.

Gaydon
Product engineering, test facilities, proving ground.

Studley
The Marketing Institute – marketing and sales training.

COVENTRY

Canley
Product engineering, design and concept engineering, commercial, external affairs.

SOUTH MIDLANDS

Cowley, Oxford
Products: assembly of Rover 800, Montego, Maestro, Body pressings and assembly of Rolls-Royce body. Body engineering, service, product training, machine tool design and manufacture.

Stratton St Margaret, Swindon
Products: body pressings, body design, tool design, and die manufacture.

WALES

Bargoed, Mid Glamorgan
Products: light presswork and componets.

PREM 19/3042.

COMPANY ADDRESSES

The Rover Group plc

LONDON
7-10 Hobart Place
London SW1W 0HH
Telephone: 01 235 4311
Telex: 926880

COVENTRY
Fletchamstead Highway
Coventry CV4 9DB
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ROVER GROUP

A British Aerospace Company

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10 DOWNING STREET
LONDON SW1A 2AA

From the Private Secretary

13 June 1989

I am writing on behalf of the Prime Minister to thank you for your letter of 25 May and for sending her the 1989 edition of Rover Group Facts and Figures.

With best wishes,

Paul Gray

Sir Graham Day

KK

ROVER GROUP

The Rover Group plc
7-10 Hobart Place
London SW1W 0HH
Telephone: 01-235 4311
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R246

25th May 1989

The Right Honourable Margaret Thatcher MP.,
House of Commons,
London,
SW1A OAA.

Dear Mrs. Thatcher

I am sending you the 1989 edition of Rover Group Facts and Figures which I believe will give you a comprehensive view of our operations in a concise and useful way.

During the course of the year we shall supplement the information from time to time to ensure that you have an up to date view of the Group and its contribution to the United Kingdom economy.

Sincerely

Graham

SIR GRAHAM DAY

CONFIDENTIAL

PAUL GRAY

16 January 1988

ROVER

The Prime Minister may be interested to see the first evidence of some commercial thinking in the management structure of the Rover Group under its new ownership.

It would appear that many of the organisational improvements which we were told 12 months ago were impossible, have now come to pass. I will not be surprised to see these moves followed by relocation of Land Rover manufacturing and assembly to existing AR sites at Longbridge and Cowley, thereby releasing the Solihull facilities for sale.

It would then only remain for Rover to withdraw from the small car market of the 90s, thereby saving all the development expenditure which we found so highly questionable, for our proposals of a year ago to have become fact. You will recall that Sir Graham Day and his team were highly dismissive of such ideas, even in the presence of the Prime Minister.

GEORGE GUISE

on either lowering domestic demand

TIMES 16/1

Slimmed-down Rover drops directorships

By Our Industrial Staff

Top management changes at Rover Group are to bring Austin Rover and Land Rover together under a single team of directors.

The 10 newly-appointed Rover directors will replace 36 directors in the old structure. Mr George Simpson, Rover's managing director, said the new structure, which will produce "significant financial savings," was designed to improve internal efficiency. He said the company could no longer afford to "invest twice" in manufacturing and engineering resources.

Vehicles will continue to be sold under the Austin Rover and Land Rover marques although Austin is soon to be dropped from the cars in favour of just Rover. Mr Simpson has brought back Mr Chris Woodwark from America, where he was sent to rescue the troubled Rover Sterling sales operation, and appointed him commercial director of Land Rover.

Mr Simpson's new appointment meant there was no job for Mr Tony Gilroy, who resigned as managing director of Land Rover in December. Mr Les Wharton, Austin Rover's former managing director, is now a director of the Rover Group.

Mr John Towers, Land Rover's manufacturing director, becomes product development director. He is the only Land Rover director promoted to the new Rover board. Mr Roland Bertodo, engineering director for Austin Rover, becomes strategic planning director.

pl cc (this page only) to Miss Carter
Mr D. Robinson 14
13/1 and return to me PLB 13/1

News Service

ROVER GROUP

RELEASE IMMEDIATE

13 JANUARY 1989

The Rover Group plc
7-10 Hobart Place
London SW1W 0HH
Telephone: 01-235 4311
Telex: 926880

New Management Structure

The Rover Group plc today (January 13) announced a single management structure for all Rover Group, Austin Rover and Land Rover activities.

Sir Graham Day, Rover Group Chairman said "The Company as a whole has progressed to the point where it is now profitable. We are now starting a very positive and ambitious phase of our development; we are planning to invest over £1,000 million during the next five years in new products across our model range and on major engineering, manufacturing and technological programmes to support these new models.

"We must manage these programmes as effectively and efficiently as possible within a streamlined organisation."

The new Rover Group management structure is as follows :

Chairman	Sir Graham Day
Managing Director	G Simpson
Austin Rover Commercial Director	K T Morley
Corporate Affairs Director	J M Pullen
Design & Concept Engineering Director	R Axe
Finance Director	H A Rose
Land Rover Commercial Director	C J S Woodwark
Manufacturing Director	A Barr
Personnel Director	F B Saundry
Product Development Director	J Towers
Quality Director	A C Curtis
Strategic Planning Director	R G Bertodo

The new structure replaces the previous management organisation within Rover Group, Austin Rover and Land Rover; the members are drawn from Rover Group, Austin Rover and Land Rover senior managers, and with the exception of commercial activities, will operate on an integrated basis across the whole Group.

Commercial activities, which include marketing and sales and relationships with dealers and customers will continue to operate as separate Austin Rover and Land Rover activities within the Group organisation.

The above management group, with the addition of N J Carver, B E Friend and L M Wharton, constitute the Board of Directors of the Rover Group. Miss S D Windridge continues as Company Secretary.

Issued by :

Corporate Affairs
Tel: 01 235 4311

ROVER GROUP

Organisation and Appointments

CHAIRMAN
MANAGING DIRECTORS
DIRECTORS WITHIN ROVER GROUP
PERSONS NOMINATED BY THE ABOVE

13 January 1989

ROVER GROUP

Further to Sir Graham Day's announcement dated 16 November 1988, a revised structure for Rover has been developed which combines the strengths of The Rover Group, Austin Rover and Land Rover into one organisation. This new organisation will support separate identities for both the Land Rover and Austin Rover product ranges in the market place whilst deriving full benefit within the Company from the integration of all other activities. The revised organisation is shown on the attached chart.

With effect from Monday, 16 January 1989, the following appointments are announced reporting to me:

COMMERCIAL DIRECTOR - AUSTIN ROVER: K T MORLEY

Kevin Morley continues with his current responsibilities for marketing, sales and customer support for the Austin Rover product range in the UK, Europe and overseas.

COMMERCIAL DIRECTOR - LAND ROVER: C J S WOODWARK

Chris Woodwark will return from his assignment with ARCONA in the United States to become responsible for marketing, sales and customer support for Land Rover and Range Rover product ranges throughout the world.

PRESIDENT - AUSTIN ROVER CARS OF NORTH AMERICA: G J MORRIS

Graham Morris will take up his new appointment in Miami on 1 February 1989, succeeding Chris Woodwark as President of ARCONA. He currently holds the position of Managing Director, Freight Rover.

MANUFACTURING DIRECTOR: A BARR

Andy Barr will now be responsible for all manufacturing and purchasing activities within Rover Group.

PRODUCT DEVELOPMENT DIRECTOR: J TOWERS

John Towers is appointed to this new position responsible for the product engineering of all Rover Group vehicles.

STRATEGIC PLANNING DIRECTOR: R G BERTODO

Roland Bertodo will be responsible for the formulation of Rover Group's forward business plan including product strategy and the initiation of collaborative arrangements. He will also manage collaborative arrangements including the existing relationships with Honda.

DESIGN AND CONCEPT ENGINEERING DIRECTOR: R AXE

Roy Axe continues to be responsible for the design and engineering of vehicles at the concept stage.

FINANCE DIRECTOR: H A ROSE

Tony Rose will now be responsible for all finance matters within Rover Group.

QUALITY DIRECTOR: A CURTIS

Alan Curtis will be responsible for setting quality standards for the Group and for carrying out quality audits. Alan Curtis will also be responsible for managing the Total Quality programme and for providing Quality leadership throughout the Company.

PERSONNEL DIRECTOR: F B SAUNDRY

Frank Saundry continues to be responsible for all personnel matters within Rover Group.

CORPORATE AFFAIRS DIRECTOR: J M PULLEN

John Pullen will be responsible for all public and product affairs matters within the Group.

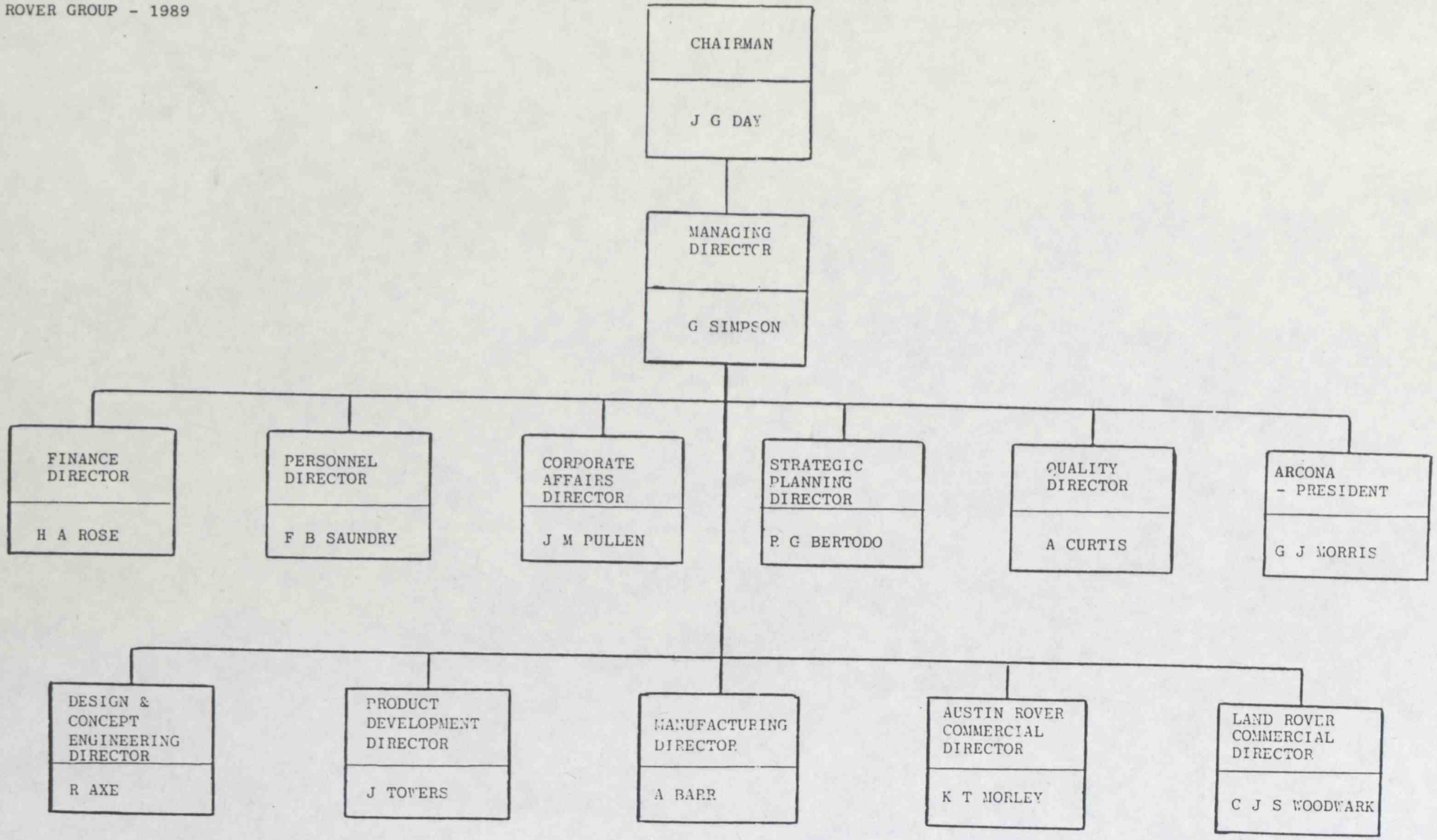
MR N J CARVER and MR L M WHARTON will take up positions as Executive Directors within the new Rover Group organisation, and their advice and experience will be available to me as well as to the Chairman.

Mike Carver has been closely involved with Honda from the inception of the relationship and he will continue to fulfil a key role working closely with Roland Bertodo and myself.

Les Wharton will be appointed to represent the Company on the Boards of a number of organisations in which Rover Group has a financial interest.

G SIMPSON
Managing Director

ROVER GROUP - 1989



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TARIFF INCREASE: RANGE ROVER

SUMMARY

1. TENFOLD INCREASE IN TARIFF IMPOSED ON RANGE ROVER. COMPANY IS SEEKING REVIEW: WE AND COMMISSION DELEGATION ARE SUPPORTING.

DETAIL

2. US CUSTOMS ISSUED ON 4 JANUARY A DECISION CLASSIFYING ONE MODEL OF SUZUKI SAMURAI FOUR-WHEEL DRIVE VEHICLE UNDER HS TARIFF HEADING 8704, QUOTE VEHICLE FOR THE TRANSPORT OF GOODS UNQUOTE, INSTEAD OF 8703, QUOTE VEHICLE PRINCIPALLY DESIGNED FOR THE TRANSPORT OF PASSENGERS UNQUOTE. DECISION WENT ON TO INSTRUCT CUSTOMS OFFICERS TO APPLY SAME CLASSIFICATION TO A LIST OF VEHICLES OF QUOTE SAME BASIC DESIGN UNQUOTE, INCLUDING RANGE ROVER (AND A VOLKSWAGEN CAMPER-TYPE MINIBUS) AS WELL AS OTHER JAPANESE FOUR-WHEEL DRIVE VEHICLES.

3. RECLASSIFICATION INCREASES TARIFFS ON RANGE ROVER FROM 2.5 PER CENT TO 25 PER CENT, RAISING COST BY 5600 DOLLARS APPROX. RANGE ROVER'S ESTIMATE (PROPRIETARY INFORMATION) IS THAT IT WILL LOSE THEM SALES OF 700-1000 VEHICLES PER YEAR, JUST AS THEY ARE BUILDING UP MARKET SHARE (SALES IN 1988 WERE 3400 CARS APPROX).

4. THE DECISION TAKES IMMEDIATE EFFECT AND WILL CATCH ABOUT 250 RANGE ROVERS ALREADY AT THE DOCK OR IN TRANSIT. IT WAS PRECEDED BY NO FORMAL HEARING NOR INDICATION OF INTENTION BY CUSTOMS.

5. THE BACKGROUND IS SOMEWHAT COMPLICATED BUT IT APPEARS THAT TO CIRCUMVENT THE JAPANESE CAR VRA CERTAIN JAPANESE MANUFACTURERS, IN PARTICULAR SUZUKI WHO HAVE A VERY SMALL QUOTA, HAVE BEEN RESORTING TO SUBTERFUGE (E.G. REMOVING REAR SEATS ETC FOR SHIPMENT, THEN REINSTALLING THEM ON ARRIVAL) TO SECURE CLASSIFICATION UNDER HS 8704 (THEY DO NOT MIND THE HIGHER DUTY). SUZUKI SOUGHT FROM CUSTOMS A CONFIRMATION THAT HS 8704 APPLIED TO THEIR SAMURAI: CUSTOMS AGREED BUT HAVE TRIED TO IMPOSE CONSISTENCY BY CLASSIFYING A NUMBER OF LOOK-ALIKES UNDER HS 8704, INCLUDING RANGE ROVER AND VOLKSWAGEN.

6. OUR VIEW, SHARED BY COMMISSION DELEGATION AND RANGE ROVER, IS THAT THE ABOVE SUGGESTS THAT OUR INTERESTS PROBABLY LIE IN KEEPING OUR DISTANCE FROM THE JAPANESE, WHOSE MANUFACTURERS HAVE

MIXED OBJECTIVES.
7. WE HAVE DISCUSSED NEXT STEPS WITH RANGE ROVER, WHO TELL US THEY CANNOT ABSORB THE INCREASED COST BEYOND THE END OF JANUARY, AND WITH THE COMMISSION DELEGATION. RANGE ROVER'S OBJECTIVES ARE, IN ORDER OF PRIORITY:

1) TO OBTAIN RELIEF FOR VEHICLES IN TRANSIT:

2) TO SEEK AN EARLY REVIEW BY CUSTOMS ADDRESSING SPECIFICALLY THEIR MODEL. (CUSTOMS HAVE PROMISED THEM A RULING BY END-JANUARY BUT HAVE WARNED THEM THAT CLASSIFICATION UNDER HS 8704 IS LIKELY TO BE CONFIRMED):

3) IF ALL ELSE FAILS, TO PERSUADE CUSTOMS TO REOPEN THE WHOLE QUESTION OF CRITERIA DISTINGUISHING PASSENGER FROM GOODS VEHICLES. THIS AT LEAST WOULD GIVE RANGE ROVER A HEARING HITHERTO DENIED, AND ROVER ASSUME THAT THE RECLASSIFICATION WOULD BE ABANDONED AND THE INCREASE SUSPENDED IN THE INTERIM.

8. THE COMMISSION DELEGATION ARE SEEKING AUTHORITY FROM BRUSSELS TO SUBMIT
A FORMAL NOTE REGISTERING PROTEST BOTH AT THE DECISION (WHICH IS PATENTLY ABSURD) AND AT THE UNFAIR AND ARBITARY MANNER IN WHICH IT HAS BEEN REACHED AND IMPLEMENTED. WE SUPPORT THIS APPROACH, INDEED ARE ENCOURAGING THE DELEGATION TO TAKE EARLY ACTION ORALLY (THEY HAVE UNDERTAKEN TO SPEAK AT SENIOR LEVEL TO CUSTOMS).

9. WE HAVE RAISED THE ISSUE AT A NUMBER OF LEVELS WITH USTR, AND WILL DO SO WITH OTHER AGENCIES ESPECIALLY TREASURY (WHO HAVE FORMAL RESPONSIBILITY FOR CUSTOMS), STATE AND COMMERCE. WE DO NOT NEED ANY PARTICULAR INSTRUCTIONS BUT WE HOPE UKREP CAN ENCOURAGE COMMISSION TO RESPOND QUICKLY AND POSITIVELY TO THE DELEGATION: SUBJECT TO YOUR AND THEIR VIEWS THERE MIGHT BE VALUE IN A BRIEF DISCUSSION AT 113 COMMITTEE.

ACLAND

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the department for Enterprise

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Our ref
Your ref
Date 9 January 1989

Prime Minister

To note the compromise agreed between Messrs Newton and Major.

RRCG
11/1

Dear John.

FREIGHT ROVER

We spoke on 29 December about this case following your letter of 23 December. I explained that the Department's inner city provision is essentially for the Task Forces and City Action Teams, and is not adequate or designed to fund RSA offers where the justification for assistance rests partly on inner city grounds. As you know the Government's policy is to use established instruments in ways which channel a higher proportion of the benefits to inner cities and their residents, rather than to devote much larger sums to instruments which are specific to inner cities. You accepted, in your letter of 23 December, that RSA could be applied in this way providing the existing criteria are met. I argued that, the question of additionality aside, the Freight Rover case was strong in every respect; and that although additionality was weak, there remained a risk that the project would not proceed without assistance. In view of the benefits the project would bring, particularly but by no means solely in furthering the aims of our inner city policies, this was a risk I felt unable to take.

DE5ACB

dti

the department for Enterprise

In response you were good enough to propose a compromise, viz that I should make an offer of £4.6m funded half from the Department's inner city provision and half from other cash-limited votes. I confirm that on this basis an offer was made to and accepted by Freight Rover last week. A pre-condition of the offer is that the company must establish a training programme which will make a significant contribution to the training of people in the neighbourhood of the project. As agreed my officials will be in touch with yours when detailed proposals for this programme have been drawn up.

I have noted your requirement that clear and testable criteria be agreed with your officials to govern the use of RSA to support inner city policies. This will be taken on board in the Department's work on this subject referred to in my Action for Cities progress report. In the meantime I must emphasise that my agreement to fund the offer to Freight Rover from outside the normal RSA provision cannot be taken as a precedent for any future cases where a project meeting RSA criteria also promises inner city benefits.

I am sending a copy of this letter to the Prime Minister.

Yours ever.
Tony.

TONY NEWTON

DE5ACB



PART 15 ends:-

CST to CDh 23/12/88

PART 16 begins:-

CDh to CST. 7/1/89



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