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CABINET

MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

STRATEGY FOR THE COAL INDUSTRY

MEMORANDUM BY THE SECRETARY OF STATE FOR ENERGY

INTRODUCTION

1. When we discussed coal strategy in July (E(79)5th meeting Item 5), I was asked to consider the steps needed to improve the medium-term financial prospects of the National Coal Board (NCB).

RETURN OF VIABILITY

2. After interest, but before Government grants of £170m, the NCB made a loss of £190m in 1978/79. Their recent Medium Term Development Plan (MTDP) forecast no improvement in financial performance. As this was unacceptable, I pressed them for proposals for achieving at least breakeven, after social grants alone, by the end of the PES period. I pressed them in particular to consider accelerating the rate of closure of uneconomic capacity, which they assumed in the MTDP to be 1½m tonnes a year (compared with an annual average of 0.8m tonnes in the past five years). Their very strongly held view is that the rate of 1½m tonnes will itself be difficult to achieve and that a faster rate would lead to very considerable political, industrial relations and marketing difficulties. The Board think that trying to achieve closures of 3m tonnes a year would so strain industrial relations that performance at continuing collieries would be depressed and the benefits of the long-term investment programme jeopardised. About 20,000 men (of whom 9,300 could be transferred) would be affected by closures at a rate of 1½m tonnes a year and about 38,000 (of whom 20,500 could be transferred)

by closures at a rate of 3m tonnes a year. Annex 1 shows the regional distribution. The Board say that doubling the rate from 1½ to 3m tonnes a year would not in fact improve their financial results during the period to 1983-4, compared with their proposals below, because of the extra redundancy and transfer costs that would have to be met and because of the loss of output which could not be made up from other pits within the period. It would however improve results after 1983-4.

3. The need to get rid of the uneconomic tail, as part of a restructuring of the industry, is not at issue, but rather the practical rate at which this can be achieved. The Board's own proposals are to plan to achieve closures at a rate of 1½m tonnes a year (and more if possible) and to make better use of existing assets by employing more men and providing additional facilities within long-life collieries. The resulting increase in colliery output of 2m tonnes by 1983/84, together with an earlier build-up of opencast, is reflected in the Board's financial forecast in Annex 2. Table 1 shows that by 1983/84 the Board should be achieving break-even after interest (on the present capital structure), after social grants, and after regional grants reduced by then to £27m (1978/79 prices). Beyond 1983/84 the Board would be expected to break-even after interest with social grants alone. Table 2 compares the Board's need for external finance with the provision in Cmnd 7439 and shows the cost to the Government of enhanced redundancy and transfer allowances (see paragraph 6 below).

4. The alternative course is to press for higher closures. The Board have provided me with a case, although they regard it as unattainable, in which the same financial improvement is achieved by 1983/84 with closures at 3m tonnes a year, but with higher social grants consequent on the higher redundancies. This is shown in Tables 2 and 3 of Annex 2. But insistence on planning a higher rate of closure than 1½m tonnes a year would, in my judgment, lead to a confrontation with the Board and quite possibly the resignation of the Chairman and other members. The closure rate would then become a matter at issue, not between the unions and the management, but the unions and the Government. The threat of a national strike, unless the Government were prepared to back down, would be likely; and the end result, apart from wider economic and political effects, could well be a much worse financial position for the industry than at present and a harder struggle to achieve break-even than with the proposals the Board have now put forward. This is not the time to take such risks. In any case our concern is with the attainment of financial viability as such rather than the means by which it is attained. I accept that the Board may not be able to achieve viability on their own prospectus but if this became apparent, we would be in a much stronger position to press for a faster phasing out of uneconomic capacity, perhaps with substantial changes on the Board.

CONTROL AND MONITORING

5. Especially if we have any doubts about the achievement of the Board's own targets, we must:

a insist that any grants which may exceptionally be agreed (eg on coking coal) in addition to those assumed in the forecasts should not relax the Board's objective, but should count towards self-financing over and above break-even.

b closely monitor the actual trend of production costs in real terms compared with the projections underlying the forecasts.

REDUNDANCY AND TRANSFER TERMS

6. The NUM have become increasingly hostile to closures, and passed a resolution at their 1976 Annual Conference to oppose all closures other than exhaustions. The previous Government did nothing to counter this attitude. Consequently to sustain a closure rate of at least 1½m tonnes a year will be difficult even with a big investment programme. The existing redundancy and transfer arrangements in the industry do nothing to discourage maximum resistance to closures. At my suggestion the NCB have therefore proposed extended arrangements (see Annex 3) to encourage the over 50's to accept early retirement and the younger men to transfer to more profitable pits. Our officials will need to study the details of these proposals and their possible repercussions, but I hope we can agree in principle that there should be substantial improvements designed to induce miners to accept closures. We can earn great credit within

the industry from a general approach on these lines as well as saving money in the long run by facilitating closures.

INVESTMENT

7. In E(EA)(79)22 I proposed that the investment programme to 1982/83 be endorsed subject to examination of the scope for cost savings. Savings of £25m a year are reflected in the external finance requirements in Table 2 of Annex 2. I propose that the investment programme to 1982/83 should now be endorsed in the usual way - in full for 1980-1 and up to 85% and 70% in the two following years. New mine projects will still come forward for separate consideration.

CAPITAL STRUCTURE

8. The case for converting some of the NCB's loan capital to equity in the form of Public Dividend Capital (PDC) was summarised in E(EA)(79)22. The Board's assets are financed virtually entirely by loan capital although private mining companies have equity finance as high as 75%. The case for some PDC is very strong, though we must see that it is not used as a soft option by the Board: the benefit should improve their self-financing rather than relax their financial target. I propose that the initial issue of PDC be limited and that, in the Coal Bill to be introduced later in the year, powers be taken to enable no more than 35% of debt to be converted to PDC initially and to permit further issues up to 50% subject to the approval of the Treasury, it being understood that these further issues should take place only when the Board have shown that they are making progress to viability.

CONCLUSIONS

9. I invite the Committee:

a to endorse the financial strategy for the NCB outlined in this paper and to accept the associated external finance requirements;

b to agree in principle to substantial improvements in redundancy and transfer terms, the details to be agreed with the Treasury following further examination;

c to approve the investment programme to 1982/83 as described in paragraph 7;

d to agree that the proposed Coal Bill should make provision for payment of grants as envisaged in the forecasts in Annex 2 and for issue of Public Dividend Capital, as outlined in paragraph 8.

D.A.R.H.

DEPARTMENT OF ENERGY
21 SEPTEMBER 1979

ANNEX 1

MEN AFFECTED AT ASSUMED ANNUAL CLOSURE RATES

(Total number of men affected over the whole period to 1983/4)

	Total Manpower (End June) 1979	1½m tonnes	(2) % of (1)	3m tonnes	(4) % of (1)
ttish	21,000	1,200	(6)	3,700	(18)
th East	33,800	6,100	(18)	10,100	(30)
kshire	65,200	3,300	(5)	3,600	(5½)
lands	62,400	2,800	(4)	3,700	(6)
tern	23,200	3,000	(13)	9,200	(40)
th Wales	27,300	3,500	(13)	7,600	(28)
at Britain	232,900	19,900	(8½)	37,900	(16)

tern

ashire	8,640	490	(6)	5,340	(62)
th Wales	1,250	550	(44)	550	(44)
erland	980	980	(100)	980	(100)
ffordshire	12,320	1,000	(8)	2,370	(19)
al Western	23,190	3,020	(13)	9,240	(40)

SFERS

er of men who could be transferred to other jobs in the industry

	Short distance	Long distance (ie to Yorkshire and Midlands)	Total
tonnes	6,900	2,400	9,300
tonnes	10,500	10,000	20,500

s not possible for the NCB at present to indicate the regional ribution of the source of the men who could be transferred long distance.

ANNEX 2

FINANCIAL EFFECTS OF PROPOSED STRATEGY

TABLE 1

£m (1978/79 prices)

Effect on NCB Profit and Loss Account

	1979/80	1980/81	1981/82	1982/83	1983/84
Operating Profit/ (Loss)	(65)	(34)	(7)	63	128
Interest	(166)	(180)	(195)	(208)	(218)
Social Grants	58	61	63	63	63
Operating Grants	55	20	18	11	-
Regional Grants	136	133	121	72	27
	18	-	-	-	-
Additional benefit					
i) from 50:50 PDC/Loans	-	81	90	97	103
ii) from 35:65 PDC/Loans	-	57	63	68	72

TABLE 2

Public Expenditure Effects

£m (1978/79 prices)

	1979/80	1980/81	1981/82	1982/83	1983/84
NCB external financing requirement (including leasing):					
(a) provision in Cmnd 7439	582	535	529	480	-
(b) 1979 FIR	664	623	608	622	622
(c) latest proposal	581	634	603	537	440
(c) - (a)	(1)	99	74	57	-
Cost of enhancing redundancy/transfer payments	5*	16	16	16	16
Increase in public expenditure over Cmnd 7439	4	115	90	73	-

* Depending on closures achieved this year.

TABLE 3

FINANCIAL EFFECTS OF 3mTONNES A YEAR CLOSURES

£m (1978/79 prices)

Profit & Loss Account	1979/80	1980/81	1981/82	1982/83	1983/84
Operating Profit/ (Loss)	(65)	(73)	(44)	33	105
Interest	(166)	(180)	(195)	(208)	(218)
Social Grants	58	78	80	81	85
Operating Grants	55	20	18	11	-
Regional Grants	136	133	121	72	27
	18	(22)	(19)	(11)	(1)

TABLE 4

£m (1978/79 prices)

Public Expenditure Effects	1979/80	1980/81	1981/82	1982/83	1983/84
NCB external financing requirement	581	668	633	560	459
Additional cost of redundancy/transfer payments *	17	54	54	54	54
Increase in public expenditure over Cmnd 7439	16	187	158	134	-

* Covers the higher number of miners made redundant and transferred as well as the enhanced level of payments.

ANNEX 3

The NCB proposals for improvements in the Redundant Mineworkers Payments Scheme (RMPS) and in the transfer grant system

Redundants

1 Men aged 55 and over now receive approximately two-thirds of their pre-redundancy earnings for three years (average about £71 per week) and then unemployment benefit equivalent plus miner's basic pension (at present about £33 per week in total) to age 65. Naturally they will fight against having to come down to this level at age 58; especially since under the early retirement scheme a man can retire at 60 and receive two-thirds of his pre-redundancy earnings up to age 65. The NCB propose that, for redundants, benefit at two-thirds of earnings should continue to age 65.

2 Men aged 50 to 54 now receive only a lump sum, maximum £1250. They would not normally be offered transfer to another pit. The NCB propose that they should have a lump sum of £150 for each year of service, in addition to the normal redundancy lump sum under the Employment Protection Act, to help them find some other way of life; and in addition, to maintain them at a reasonable standard if they cannot get another job, continued payment to age 65 equivalent to unemployment benefit and earnings related supplement. At present this would average about £42.50 per week. The RMPS lump sum would average about £4500.

3 Men under age 35 now receive nothing from the RMPS. Those aged 35 to 49 receive a lump sum maximum £1250. The NCB propose that all men aged 20 to 49 should receive a lump sum of £150 for each year of service, in addition to the normal redundancy lump sum under the Employment Protection Act. The average RMPS lump sum would be about £2250.

Transferees

4 At present men transferred to other pits within daily travelling distance receive no special allowances. The Board propose that they should receive:-

a) a disturbance allowance of up to £600 depending on their length of service, and

b) retention payments of £200 after six, twelve and twenty four months in their new jobs.

Those transferring to pits outside daily travelling distance should receive:

a) a lump sum equivalent to the normal redundancy lump sum under the Employment Protection Act;

b) a lump sum equivalent to the lump sum under the RMPS or £150 for each year of service, (average say £3000);

c) a disturbance allowance of £2000;

d) allowances to cover the cost of moving, increased rent etc;

e) retention payments of £500 after six months and a further £250 after twelve and twenty-four months in their new jobs.

5 Those who cannot transfer for one reason or another must be given reasonable compensation to make redundancy tolerable. However it is vital to encourage as many of the younger skilled men as possible to transfer to the new pits, and also to more highly productive pits. But they will be less inclined to transfer if they do not get terminal payments equivalent to the redundancy payments for which they would qualify by staying put.

6 This means that ways must be found of permitting these terminal payments to be paid tax free. We understand that regarding them as a "golden handshake" from the pit where they were formerly employed might be one way of achieving this. (Formally, men are employed by the pit at which they work and not as such by the National Coal Board. So when the pit closes their contract of employment formally ceases.)

Costs (1978/79 prices)

The following table shows the total costs falling on the Department for the five years to 1983/84.

	No. of men	Cost £m	Existing cost £m	Additional cost £m
RMPS lump sums:				
a) men aged under 50	4,700	10	2	8
b) men aged 50 to 54	8,850	39	10	29
RMPS weekly benefit:				
a) men aged 50 to 54		18	-	18
b) men aged 55 to 64	9,950	54	47	7
Employment Protection Act lump sums		15	15	-
Short distance transfers	6,900	4	-	4
Long distance transfers	2,400	12	4	8
Non-industrial transfers		2	-	2
Totals		154	78	76

Notes

1 The RMPS is financed 100% by the Department. The other sums represent the Department's 50% contributions under the Coal Industry Act 1977.

2 If cokeworkers, as is proposed, are included in the RMPS on the revised basis it would add some £4m to these costs.