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My ref:
Your ref:

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Dear Chancellor of the Exchequer

INDUSTRIAL SUPPORT

In my letter of 14 August I confined myself to general comments on the ideas put forward in Keith Joseph's letter of 8 August.

In paragraph 16 of his letter he turned to measures designed to encourage companies to maintain discretionary expenditure which would be distinct from any general or discriminatory relief from pressures on liquidity. Their aim would be to counteract the undesirable effects of the liquidity squeeze, by maintaining "seed corn" expenditure on which future prosperity demands: and they would be taken under existing powers.

I feel strongly that such measures should include - indeed ought to have included in the past - assistance specifically directed towards environmental improvement, including the recycling of waste materials where I believe new initiatives are required. Such a move would have wide public appeal and it would recognise the need for industry to put itself on a more competitive footing, in terms of technical progress and "clean" technologies generally, with other EC member states where the political and governmental pressures have on the whole been stronger than in this country.

I therefore asked my officials to prepare a paper setting out some initial suggestions. A copy of this is enclosed. I should be grateful, if after such further discussions as may be required between officials, you will take them into account in the preparation of your paper for E Committee.

I am copying this letter to the other recipients of Keith Joseph's letter of 8 August.

Yours sincerely

J. P. Channing

for MICHAEL HESELTINE
(approved by the Secretary of State
and signed in his absence)

CONFIDENTIAL

FINANCIAL ASSISTANCE TO INDUSTRY FOR ENVIRONMENTAL PURPOSES

1. This paper considers the scope for introducing measures for financial assistance to industry, related to the achievement of environmental objectives.

PRESENT POSITION AND BACKGROUND

2. At present the UK has no system of grants to industry specifically related to the achievement of pollution control objectives. Limited assistance may be available where grants are being paid for other purposes (eg industrial improvement), and grants are paid for research and development in some fields (in particular waste recovery equipment).

3. The UK has been a strong advocate of the "polluter pays principle", on grounds of equity and efficiency in a domestic context, and because of its contribution to the reduction of trade distortion. Ppp is also generally supported by other countries, and there are recommendations relating to it both in the EC and the OECD. However, most other EC countries take a more flexible view than we do of ppp, and provide assistance to industry in various ways for pollution control purposes.

4. A note on the EC recommendation on ppp is at Annex A. Any proposals for new schemes of financial assistance would need to be cleared with the EC Commission, which has the power to keep under review all systems of aid, and to find whether aids are compatible with the Treaty.

OBJECTIVES OF GRANT SCHEMES

5. In terms of environmental policies, the possible objectives of introducing a system of financial assistance to industry might include:

- a. to help industry to maintain the rate of progress of environmental improvement;
- b. to avoid putting UK industry at a disadvantage vis-a-vis their competitors in other EC countries;
- c. to encourage the saving of scarce resources;
- d. to encourage technological innovation in the pollution control field, and thereby increase the competitiveness of British industry at home and abroad.

6. Proposals for financial assistance would need also to be looked at in relation to the development of industrial support measures generally. Measures would need to be framed, and implemented, in close co-operation between the Environment departments and DOI, so that their operation should strike the best balance in achieving both environmental and industrial objectives.

POSSIBLE METHODS OF INTRODUCING ASSISTANCE

7. Four possible methods for providing assistance have so far been identified. All of these could be operated on the basis of existing statutory powers (principally Section 8 of the Industry Act 1972, and Section 5 of the Science and Technology Act 1965). The four methods are:

- a. Modification of general grant schemes, so as to remove the limit on financial assistance for pollution control measures forming part of a larger project.
- b. Specific grants for plant designed to recover or re-use waste materials.
- c. Grants to assist the development and application of environmentally clean products and processes.
- d. A scheme of specific grants towards the cost of pollution control measures.

Modification of existing grant schemes

8. Industrial projects frequently involve the installation of pollution control equipment etc. The pollution control element

of the scheme will usually represent a small part of the total cost; but in some cases it may be a substantial element. However, the present practice is to limit the pollution control element of any scheme which is eligible for grant to 15-20% of the total cost.

9. Removal of this (administratively imposed) limitation would help to meet both environmental and industrial objectives. There is, in any case, a case for saying that such measures ought to be regarded as an integral part of industrial projects. Removal of the limitation would not conflict with the EC recommendation on the ppp.

Grants for plant designed to recover or re-use waste materials

10. Grants could be paid (under the Industry Act) to firms which install plant for the recovery or further use of waste material. This would be, to some extent, an extension of existing practice. There has been a scheme, for example, for the paper industry, to encourage the production of recycled paper. Further ways in which such grants might be used include:

- a. encouraging the setting up (perhaps on a co-operative basis) of schemes for the sorting and recycling of solid waste where the combined economic benefit, to the local authority and to industry, justifies this.
- b. encouragement of measures within industry to increase the recovery of materials which are at present dispersed into the environment. This might cover not only solid wastes, but materials which are at present emitted to air or discharged to water.

11. Measures of this kind would help to meet the general objective of conserving scarce resources, and would also bring environmental benefits - for example, reduction in solid (and possibly toxic) wastes, improvements in air and water quality, and avoidance of problems which arise from the accumulation of heavy metals in sewage sludge. There would be no clash with EC requirements.

Cleen Technologies

12. The Product and Process Development Scheme, under Section 5 of the Science and Technology Act 1965, enables assistance to be given in order to promote the design, development, and launching of a new or improved product or process. Consideration might be given to the introduction of environmental criteria into the operation of this scheme, and grants might be given specifically to promote the development and application of environmentally clean products and processes, including quiet machinery (this would bring environmental benefits, but the immediate beneficiaries might be workers in factories, and HSE would therefore need to be involved).

13. In addition to the specific assistance available under the Product and Process Development Scheme, firms producing pollution control equipment are eligible, like other firms, for assistance under the Industry Act. The industry has considerable surplus capacity; and although 50% of output is exported, profit margins are understood to be low. Again, a specific environmental dimension might be introduced into the operation of general schemes of assistance so as to help the pollution control equipment industry.

14. Measures to encourage the development and application of clean products and processes, and to help the pollution control equipment industry generally, would bring environmental benefits. There should also be advantages in terms of industrial support. In particular such assistance would help UK industry to compete when there is a growing overseas market as environmental standards are raised in other countries. This change in the implementation of existing schemes of assistance would not present any problem in the EC context.

Specific grants for pollution control measures

15. In addition to the above measures for introducing environmental considerations into existing schemes of financial assistance, there is scope for a new scheme of specific grants towards the cost of pollution control measures, within the limits (15% of the cost)

laid down in the EC interpretation of the polluter pays principle. Such specific grants would need to be administered by the Environment departments, in close consultation with DOI.

16. Grants might be payable towards the costs of air pollution control measures in industrial premises which come under the control of the Alkali Inspectorate. Capital expenditure in this field in 1978 is thought to have been running at about £100 million a year, and the Alkali Inspectorate, which takes account of economic considerations in determining the "best practicable means" to be adopted at individual plants, is finding that firms are having increasing difficulty in meeting their requirements. If a grant were available, this could be taken into account by the Inspectorate in judging what would be "practicable" in any particular case.

17. A further possibility in relation to air pollution would be to provide grants for new plant needed to enable existing works to achieve the reduction in emissions required to meet the standards laid down in the recent EC directive on air quality limit values for sulphur dioxide and suspended particulates. Such grants might be available for non-registered processes (ie those controlled by local authorities rather than the Alkali Inspectorate). Availability of grants would need to be limited so as to concentrate funds on the few areas where industrial emissions of sulphur dioxide present particular problems.

18. Grants might be made available also towards tackling problems of water pollution. Here, discharges by industrial firms are generally of less significance than sewage discharges, whose improvement is a matter of increased expenditure by water authorities. However, it should be possible to develop criteria in relation to industrial discharges to encourage early achievement of river quality objectives (on a selective basis in view of the greater significance of sewage discharges), including compliance with the proposed EC directive on mercury discharges from the chloralkali industry.

19. A rough draft outline of a possible scheme of grants is at Annex B. Although such a scheme could operate within the limits accepted by the EC, as conforming with ppp, careful presentation would be necessary to meet possible objections from industry that financial assistance might be used as a lever for imposing more stringent environmental standards and that grant limited to 15% would not compensate for this.

20. In fact, the statutory basis of "best practicable means" for processes controlled by the Alkali Inspectorate, and the general acceptance of the philosophy of bpm in other fields, should ensure that the existence of a grant was not used as a means of justifying the tightening of standards in such a way as to put unacceptable burdens on industry. New standards would still be set with regard to the ability of industry to meet them - taking into account the new grant where it was available. It would also be important to emphasise that the scheme was based on the need to maintain the present rate of progress of environmental improvement.

FINANCIAL IMPLICATIONS

21. No detailed assessment of financial implications can be made until the ideas have been the subject of further inter-departmental discussion. In particular, the implications of the first three options need to be considered with DOI, in the light of their experience of operating the existing schemes. So far as specific pollution grants are concerned, a worthwhile scheme might be mounted on the basis of annual expenditure of the order of £10 million.

22. For present purposes a working assumption might be that the total annual cost of all the measures outlined above might be up to £25 million.

STAFFING IMPLICATIONS

23. A detailed assessment of staffing implications must also depend on further consultation. For pollution control grants, such consultation would need to involve regional water authorities and local authorities, as well as Government departments.

24. In principle, adoption of the first 3 options should not have significant staffing implications. A scheme of specific pollution grants would, however, call for some extra staff (perhaps 4) in DOE, and would also put some extra burden on DOI, and on the Alaska Inspectorate, regional water authorities, and local authorities.

EC RESTRICTIONS ON AID TO INDUSTRY

1. Financial assistance to industry in EC Member States has to conform to Community rules. The Commission, as guardian of the Treaty, has to be informed of any plans for new aids, in time for it to comment before such plans are implemented.
2. The general presumption is against aid to industry, which could produce trade distortions. However, Article 92 of the Treaty provides that aid may be given where there would otherwise be serious economic disturbance or high social cost.
3. In the pollution field, the Community subscribes to the "polluter pays principle" (ppp). The EC Environmental Action Programme states that the cost of preventing and eliminating nuisances must, as a matter of principle, be borne by the polluter.
4. The interpretation of ppp is set out in a Commission memorandum of 1974. In this the Commission stated its willingness to approve schemes for payments up to 31 December 1980 to finance investment needed to enable plants in operation on 1 January 1975 to meet new major environmental protection obligations. The memorandum also provided for a progressive reduction in the percentage grant payable; the maximum proportion of new investment (excluding any investment that would also increase production capacity) which could be covered by aid was set at 45% in 1975/76, 30% in 1977/78, and 15% in 1979/80.
5. Under the 1974 Memorandum, schemes for financial assistance would have to end by 31 December 1980. However, a further memorandum of July 1980 extends the period during which assistance may be given to 31 December 1986. The rate of assistance continues to be limited to 15%; and the plant concerned must have been in operation for at least two years before the new environmental protection obligations came into force (in place of the 1975 cut-off date).

INVESTMENT IN ENVIRONMENTAL QUALITY

1. The object of the scheme is to accelerate improvements in environmental quality.
2. Assistance will be given under section 8 of the Industry Act 1972.

Criteria

3. To qualify for assistance the project must lead to an earlier achievement than would otherwise be possible by plants not less than two years old of standards set for environmental improvement. The scheme would be selective and applicable to activities in any sector of pollution. Possibilities are:-

- (i) projects at plants registered under the Alkali Acts to accelerate the introduction of better pollution control equipment;
- (ii) projects which will assist in complying with EC directives; and
- (iii) projects which help to bring forward achievement of river quality objectives.

Scale of Project

4. The project costs (i.e. fixed capital and working capital) are not less than appropriate de minimis level to be inserted

Support of pollution control authority

5. The application for assistance must be supported by confirmation from the relevant pollution control authority that the project accords with the criteria in paragraph 3 (i) (ii) or (iii) above.

Technical feasibility

6. An application must be supported by an independent assessment of the technical feasibility of the project, except where confirmation can be provided from the relevant pollution control authority that in their view the project is technically feasible.

Rate of grant

7. Grants of 15% will be paid towards the project costs.
8. Where a consultant is engaged in drawing up a proposal, grant will be paid at the rate of 50% of agreed consultancy fees for inspections and advice required in preparing a proposal and for supervising and inspecting work after a proposal has been accepted.

Applications

9. Applications are to made to, and will be processed by DOE.
10. DOI's Industrial Development Unit will make an appraisal of commercial viability where project costs total £..... or more. These cases will be referred to DOI's Industrial Development Advisory Board. Where the project costs are less than this, the cases will be considered by a Departmental Projects Management Committee which will include DOI. (This Committee will also exercise a general oversight of the scheme).
11. Grants in excess of £25,000 need clearance with DC; this would be negotiated by DOI/DOE.

Payment of grant and monitoring

12. Final payment of grant will be subject to confirmation that the project is operating satisfactorily. Any necessary monitoring will be undertaken by DOE, or by the pollution control authority on its behalf. In the event of the project being suspended with £ years of completion, payment of grant may be recoverable.

Financial responsibility

13. The accounting Officer DOE will be accountable for monies paid out by DOE under the scheme.

Scotland, Wales, Northern Ireland

14. The scheme will extend to these countries, where Departmental responsibilities will be with SDD, Welsh Office and DOE Northern Ireland.

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