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PRIME MINISTER

AGRs and the Government's Nuclear Policy
(E(79) 54 and E(80) 30)

(Mr. Howell's minute to you of 31st March,
Mr. Younger's minute to you of 2nd April
and the Report by officials sent to you under
cover of my minute of today's date)

BACKGROUND

E had a substantial discussion of nuclear power policy in October last (E(79) 13th Meeting, Item 1), based on a major paper by the Secretary of State for Energy (E(79) 54) which was largely concerned with a long-term ordering programme for nuclear stations, the role of the PWR and matters connected with the organisation of the nuclear industry. That paper took for granted the continuation of work on the Heysham II and Torness AGR stations which had already been authorised. On 18th December Mr. Howell made a statement to the House reflecting the conclusions of the E discussion. He referred to the existing AGR orders in the following terms:-

"The last Government authorised the CEGB and the SSEB to begin work at once with a view to ordering one advanced gas-cooled reactor station each as soon as possible. This is in hand."

2. Earlier this year, when the problems the electricity supply industry faced in living within its external financial limits (EFLs) came to notice, you asked the CPRS to look into the need for the Heysham II and Torness stations and to report back. Their report (E(80) 30) was considered by E on 24th March (E(80) 11th Meeting, Item 3). The CPRS recommended that the Heysham II and Torness stations "should go ahead as planned". Colleagues did not feel able to come to a decision on this recommendation without further information, and you asked officials to produce additional back-up material quickly for consideration by the Ministers immediately concerned under your chairmanship. I sent you the additional information earlier today, and your meeting is to take place at 12.30 pm tomorrow. In addition Mr. Howell has

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sent you a minute (dated 31st March) urging that continuation of work on the Heysham II and Torness AGR stations should be confirmed without delay. His arguments are partly political and partly industrial. Mr. Younger, in his minute of 2nd April argues strongly in support of Mr. Howell's view.

3. Given the mass of paper now available to Ministers, it may be helpful if I seek to pull out the central thread of the argument. Briefly:-

(a) In so far as financial appraisal of projects of this size and duration can have meaning, that for Heysham II (described in Annex 3 of the officials' paper) appears to be robust. The financial argument for it does not rest on questions of generating capacity (we have plenty of that), but on the cost savings it will provide when it backs older and more expensive generating capacity out of the system. The financial evaluation of Torness was made at an earlier stage when it was thought to be needed on capacity grounds in the Scottish system. Reductions in forecast electricity demand are now tending to shift the arguments for Torness from a capacity to a cost-saving basis as with Heysham II. There is no reason to doubt that on these grounds it will prove equally robust, though, for certainty, officials of the Treasury, the Scottish Office and the Department of Energy are seeking, with the SSEB, to update the Torness arithmetic. It is hoped that the results of this work will be available shortly after Easter.

(b) The above argument assumes the validity of the financial appraisals made by the electricity supply authorities. Doubt was expressed at the last meeting of E whether this assumption could properly be made. There are three elements in such appraisals: the methodology, the external assumptions (e.g. on future energy prices) and the internal assumptions (construction costs etc.). The Treasury satisfied itself last year that the CEGB's appraisal methodology was acceptable. The external assumptions are regarded as reasonable by Departments. The internal assumptions are not checkable within the present

No - very bad costing)

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framework of relations with the electricity supply authorities.

Without a major change in those relationships the Government has to take them on trust. To do otherwise would involve the Government in taking the industry's investment decisions from it.

- (c) As of now the only nuclear option open to the Government is to build AGRs. Mr. Howell's earlier hopes of ordering a first PWR in 1982 now appear unrealistic. Annex 1 to the latest report by officials describes the necessary sequence of events. An order in 1983 is possible, but could even slip beyond then. Thus if the Heysham II and Torness AGRs are cancelled it is unlikely that any new nuclear orders can be placed much before the end of this Parliament. A hiatus of this kind would not unduly damage our ability to order PWRs at a later date but, with other AGR work coming to an end, would be likely to do considerable damage to our ability to order further AGRs. A decision to cancel would therefore be tantamount to, or would be represented as, a decision to abandon the AGR and place all our future nuclear hopes on the PWR.
- (d) A decision to defer, rather than cancel, one or both of the new AGRs would be likely to be almost as damaging to confidence in the plant-manufacturing industry as outright cancellation. As Annex 6 shows, a wide range of firms are involved and, quite apart from immediate damage, many would be likely to adopt a "once bitten twice shy" attitude to future nuclear, and nuclear-related business.
- (e) In short, cancellation or deferment of Heysham II and Torness would inflict severe, and possibly mortal, damage to our ability to build AGRs in circumstances where we cannot order a PWR until 1983 at the earliest, and cannot be sure that we will ever be able (or want) to order them (quite apart from the possibility of another Three Mile Island, it is at least possible that the additional safety requirements which the NII may place on PWRs when they have completed their examination will alter the balance of economic advantage between them and AGRs).

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4. Three other issues, touched on in the E discussion on 24th March, are dealt with in the report by officials:-

- (a) Safety. You will remember that Mr. Heseltine expressed some doubt about the political acceptability of the safety formulation on AGRs set out in the Chief Inspector of Nuclear Installations letters attached to the CPRS report (E(80) 30). Annex 8 of the report by officials deals with this. The position seems secure, but the continuing discussions suggested in the Annex (and originally recommended by the CPRS in their paper) would provide a useful additional assurance.
- (b) Drax B. The possibility of saving money by cancelling Drax B was mentioned. This is dealt with in paragraph 15 of the report by officials and in Annex 9. The conclusion that Drax B should be allowed to go ahead seems right.
- (c) Alternative work for the plant-makers. The possibility of finding alternative work for the plant-makers if Heysham II and Torness were cancelled or deferred is dealt with in paragraph 12 of the officials' report. It does not appear to provide a realistic substitute to work on the stations.

HANDLING

5. You might begin by recalling the background and then invite Mr. Howell to lead off. The objective will be to see whether a consensus can be reached on the continuation, or cancellation, of Heysham II and Torness. Other issues contribute, but this is the central question.

6. Assuming that a consensus is reached, there remains the question of further handling. If the view of the group favours cancellation, or is hopelessly split, the issue will clearly have to go back to E (the next meeting being scheduled for 16th April). If on the other hand the consensus is in favour of allowing the orders to proceed as planned, Mr. Howell will certainly argue for an early announcement based on that decision without further reference to E. You will have to judge whether to accept this. The further work being done on the Torness costings would provide an excuse for deferment of final decisions should an excuse be needed. Equally, however, given that a decision in favour of continuing with Heysham II and Torness would be a confirmation of existing policy, you could let Mr. Howell have his way.

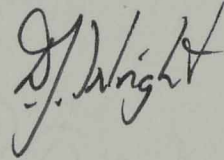
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CONCLUSION

7. Subject to discussion the group can:-

Either: (i) confirm Heysham II and Torness and invite Mr. Howell to make an early announcement;

Or: (ii) refer the issue back, with whatever recommendations reflect the discussion, to E for final decision on 16th April. In this case you could either invite Mr. Howell to put a further paper to E or you could invite me to produce a paper summarising the issues.



(Robert Armstrong)

(approved by Sir Robert Armstrong
and signed in his absence)

2nd April 1980