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Prime Minister

The Policy Unit will be putting advice to you on this. Pl. see Robin Ibb's note (attached) & and Rbt Armstrong's earlier note. (attached) Do you wish to discuss with the small group of Ministers? Given your full diary* it would probably have to be after Easter. MCS 17/3

* and Mr Jenkin's visit to N America

Agreed MT

PRIME MINISTER

BL'S FUTURE STRUCTURE

At your meeting on 14 January, it was agreed that the Government should seek independent advice on the BL Board's proposal on future structure. The Corporate Consulting Group (CCG) were retained, and they have now completed their study. I attach a copy of their report, which has been seen by the BL Board. I also attach a restricted annex containing the consultants' appraisals of the present Board members which has not, of course, been seen by BL; I have some reservation about some of the personal appraisals, which seem to me based on relatively slight acquaintance.

2 The study has centred on the only two options the consultants considered viable:

(a) the BL Board's proposals to split the present organisation into two separate companies, each owned directly by the Department of Industry; and

(b) to retain the present unified structure as a holding company with a number of independent business units.

The consultants did consider the possibility of splitting BL into four independent companies instead of two; but concluded that the interdependencies and synergy between the Cars Group and Unipart (which they saw as permanent), and in the short to medium term between Land Rover and the Leyland Group, precluded this option.

3 The CCG's conclusions are set out on pages 9 and 10 of their report. The principal ones are:

(a) both of the structures they considered are potentially viable;

(b) since the critical issues facing BL remain large, there is a continuing leadership requirement of the **most substantial kind,** which might not be adequately met by the present Chief Executives (Messrs Andrews and Horrocks) with only part-time Chairmen;

(c) in most respects a unified structure would be more resilient and manageable, though the consultants agree that splitting the company into two would somewhat reduce the risk of industrial relations trouble spreading from one side to the other;

(d) Land Rover is the only part of BL which offers much hope of privatisation within the next two years,* and

* Annex J of their report indicates how limited the scope for privatisation is.

the Board's proposal to split the company into two could be an impediment to achieving this, primarily because the Board of the "Commercial" company (Land Rover + Leyland Group) would be more reluctant to part with half their empire than the Board of the unified company to part with a much smaller part of the whole.

The consultants therefore advocate retention of the present structure with a full-time Chairman of high calibre, though they point out that if such a person cannot be found this would substantially reduce the balance of advantage in favour of this option. As an alternative, they suggest that Sir Michael could become part-time Chairman of the unified company.

4 Robin Ibbs and I have discussed the report, first with the consultants and subsequently at a meeting with Sir Michael Edwardes at which the consultants were present. Sir Michael (and his Board) were highly critical of the report, and prepared in advance a critique which claimed that the consultants had made a series of unsound "second guesses" of the Board's commercial judgements about the future management of the company, and two unsound and unsubstantiated assumptions relating to the privatisation of Land Rover. A copy of this critique is attached. Sir Michael has also made it clear to me that he would not be prepared to stay on after the end of this year as a

part-time Chairman of BL, since he is quite convinced that splitting the company into two is the right way to meet the Government's objectives for it, namely the achievement of recovery, limitation of Government funding and privatisation. The main arguments against the line taken by the consultants are as follows:

a) the present unified structure of BL magnifies and dramatises the problems of the company. The bad image of 'British Leyland' lingers on, there is always strong media interest in the company, and there is still a tendency to 'knock it';

b) as we saw in the pay dispute last November, there is a great risk of industrial relations problems in the Cars Group spilling over into Land Rover. This will be only partially removed if Land Rover is taken out of the Cars bargaining arrangements, but would be completely removed if BL were split into two;

c) two smaller companies would be easier to manage than one and the financial exposure of the company and the Government would be less if there were a disastrous strike in one or other of the two companies than if the whole company went down. The existence of two separate companies would also lessen the impact of such a disaster on the surviving company's dealers, customers, bankers, collaborators, and potential private investors.

5 For these reasons, the Board remain convinced that their original proposal represents the best way forward for the company. This presents us with a very difficult choice. Either we can build on what has already been achieved by the present Board and allow them to continue with their present strategy under the new structure (the Board have given a firm commitment that they will not seek any further Government money beyond the £150m of equity identified in the last two Corporate Plans for 1983/84 and 1984/85); or we can go down the route suggested by the consultants, try to find a new Chairman and a new Board and allow them time to work out a new strategy. It would, in fact, be extremely difficult to find a suitable successor to Sir Michael Edwardes in a unified structure. Moreover, there would be risks attaching to discontinuity of management, the risk that the unions would seek to challenge the situation, and the risk that a new Chairman would not feel the same commitment as the present one does, not to seek further large scale finance to keep BL going. The difficulties in finding a new Board willing to take over from the present one at the end of this year would be increased still further if it became known that the latter had been overruled by the Government on a matter which they (the present Board) regarded as of crucial importance.

6 The vital aspect of the whole problem is whether the BL Board's proposal would, as the consultants suggest, be an impediment to early privatisation of Land Rover. With this in mind, I asked Sir Michael when I met him to consider what new commitment his Board would be able to give the Government about the early disposal of Land Rover. He replied to me on 11 March, and I attach a copy of his letter. In the third paragraph of this letter he says that BL are pressing ahead with the preparations foreshadowed in the 1982 Corporate Plan for the introduction of private equity capital into Land Rover with the intention of achieving this within the next two years. In addition, and following the establishment on 1 January 1982 of Land Rover as a separate company within the BL Group, the Board has now commissioned further work (which I understand will involve the collaboration of Hill Samuel) on the feasibility of total privatisation of Land Rover at the earliest opportunity. This is the first time that the Board has been willing to contemplate such a possibility - though as yet without commitment - and I think this represents a major concession on their part. ??

7 In view of this, and also of the absolute commitment in the letter that the new Boards (based on the present Board membership) would stick to the limitations on Government funding envisaged in the 1981 and 1982 Corporate Plans, I recommend that we should agree to the BL Board's proposed new structure for the

company.

8 I am advised that simple primary legislation would be needed to regularise this position; and indeed that it would be desirable that Second Reading should have taken place before the split is carried out. If we decide to proceed with the legislation on the BTG, that Bill would provide a suitable opportunity.

9 I am sending copies of this minute and enclosures to the Chancellor of the Exchequer, the Secretaries of State for Trade and Employment, and to Sir Robert Armstrong and Mr Ibbs.

PJ

P J

16 March 1982

Department of Industry

TELEPHONE
01-486 6000

35-38 PORTMAN SQUARE

LONDON W1H 0HQ

FROM SIR MICHAEL EDWARDES

11th March 1982

The Rt.Hon. Patrick Jenkin, MP,
Secretary of State for Industry,
Ashdown House,
123 Victoria Street,
London SW1.

STRICTLY CONFIDENTIAL

JWB 12/3

TO Mr Bofield
FOR [illegible]
DRAFT REPLY (IF
APPROPRIATE)
PLEASE BY:
NOON
18/3/82

PS/NL
PS/JW
PS/SEC
Mr Marge
Mr Mountfield

Dear Secretary of State.

In the light of the consultants' report on BL's future structure and of our discussion on 9th March, the Board has given further thought to the aspects of its organisational proposals which bear most closely on the Government's main objectives as we understand them - i.e. the achievement of recovery, the limitation of Government funding, and privatisation.

We believe that each of these objectives can be achieved with less risk by a split into two companies than within a unified structure:-

1. We have argued that a two-company structure will reduce our present vulnerability to industrial relations crises, as well as improving our commercial prospects in other areas such as collaboration. An even more important factor underpinning the Corporate Plans of our various businesses would be the continuity at Board and top management level which the Board's proposal offers and which in turn would reduce the risk of an exodus of the senior management of our operating companies. As you know, I am willing to stay as a non-executive director of both of the new companies if this is considered helpful.

Continued

2. The continuity between the present Board and the Boards of the two new companies will serve to maintain our absolute commitment to the limitations on Government funding envisaged in the 1981 and 1982 Corporate Plans. The Board reiterated this commitment at its meeting on 10th March.

3. As I have already emphasised to you, the Board is fully committed to the free enterprise philosophy and shares the Government's objectives which include the return of BL's businesses to the private sector as soon as practicable. The consultants' report has indicated that Land Rover provides the best prospect of progress towards this objective in the short term but that there are substantial interdependencies between Land Rover and Leyland Trucks which need to be taken into account. We are pressing ahead with preparations for the introduction of private equity capital into Land Rover, as envisaged in the 1982 Corporate Plan, with the intention of implementation within the next two years. Further progress has been made since submission of the Plan, with the establishment of the Land Rover Group as a legal entity on 1st January 1982 and the decision (soon to be announced to the trade unions) to separate Land Rover from the BL Cars bargaining unit this year. In addition, the Board has now commissioned further work on the implications and feasibility of total privatisation of Land Rover. This work will include examination of the earliest sensible timing on a variety of assumptions about the method to be adopted for the transfer of ownership and about the economic environment. You have the Board's assurance that the fruits of this work, as agreed with the Government, will be carried through under the new structure which we propose.

Yours sincerely,
Michael Edwardes

LETTERCODE/SERIES PREM 19 PIECE/ITEM 803 (one piece/item number)	Date and sign
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26th February 1982

REPORT ON THE FUTURE ORGANISATION STRUCTURE OF BL

CONTENTS

EXHIBITS

Corporate Consulting Group

REPORT ON THE FUTURE ORGANISATION STRUCTURE OF BL

1 BL's proposal

1.1 The Board proposal is to split BL into two companies with their own Boards, each with a part time Non-Executive Chairman.

1.2 The Non-Executive Directors as a group are strongly committed to the proposal. The extent of their individual commitment varies. They are all sensitive to having their commercial judgment 'second-guessed'.

1.3 Sir Michael Edwardes sees the split into two companies as a natural extension of the decentralisation which has already occurred. The two Executive Directors also support the proposal, with provisos concerning the choice of Chairmen and the objectives of the new companies.

2 Interdependencies

2.1 The realism of fragmentation of the corporate structure whether into two companies, or more as has been suggested might apply to Cars, is conditioned by the extent of interdependencies between the business components. These are such as to restrict for the immediate future the options for corporate structure to two.

2.2 The interdependencies between Cars and Commercial are not sufficient to invalidate the proposed split into two companies. There are, however, risks and potential loss of synergy, arising from the separation of Land Rover from Cars.

2.3 Jaguar has extensive interdependencies with Cars and the benefits of the common franchise to Volume Cars would be lost by separation in advance of a consolidation in the recovery of Volume Cars.

2.4 Unipart is a service business integral to Volume Cars and makes no commercial sense as a wholly separate business, except in the event of the liquidation of Cars, when it would have some residual value as a diminishing trade.

2.5 There are substantial interdependencies between the two components, Leyland and Land Rover, both in the UK and overseas. Both businesses, particularly Leyland, are at a fragile stage in their recoveries and changes which do not carry clear bottom line benefits would be difficult to justify. That fragility reduces as their business plans are accomplished and, by end 1983, Land Rover in particular could be approaching a position of viability and self-sufficiency of systems. At that time the further separation of the Land Rover organisation would be possible without excessive risk to either component and pave the way for early privatisation.

2.6 In the longer term, assuming business outcomes substantially as envisaged in the '82 Plan, Volume Cars and Unipart, Jaguar, Land Rover and Leyland could all have achieved a level of self-sufficiency to achieve further fragmentation of the corporate structure, if considered desirable.

3 The options

3.1 The immediate options in terms of corporate structure are therefore confined to two - the preservation of a unified structure, containing a number of independent business units, or the separation of the present structure into two companies.

3.2 The case put forward by BL for splitting the Company into two rests essentially on two arguments. First, it claims to address the issues of manageability and commercial direction better than any other; second, it reduces the vulnerability of the whole company to the effects of a crisis arising in one of the parts in terms of financing and confidence. It also holds that the split would not impede privatisation, and solves the problem of succession to Sir Michael Edwardes.

3.3 The case for maintaining a unified structure rests on three main points. First, the size of the issues confronting BL, as far ahead as one can see, demand the highest possible leadership configuration in succession to Sir Michael Edwardes and are too large for the positions of part time Non-Executive Chairmen to be tenable; second, the likelihood of recurrent crises requires a resilient structure, which preserves the widest possible range of options for the Board and facilitates the maximum degree of objectivity and realism; third, it facilitates the pursuit of privatisation. It is also held that the principal vulnerabilities can be addressed largely without recourse to structural change.

4 The key issues

4.1 The commercial background against which either structure would operate will continue to be weak and full of uncertainty. It is, however, different to the heritage assumed by Sir Michael Edwardes. The serious financial condition at the end of 1977 did not reflect the full extent of the underlying bankruptcy of the business. Plant and products were out of date, facilities needed rationalising, costs were grossly uncompetitive and organisation had become excessively centralised. As a result, market shares were declining, cashflow was negative and management had lost its nerve and its will to manage.

4.2 Since that time shareholders funds of about £1 billion have been put in to finance losses,to rationalise facilities and products, and to reduce the workforce by some 75,000. The Metro has been successfully launched and a number of collaboration deals have been concluded or are in negotiation.

4.3 Perhaps the most striking manifestation of renewal has been the restoration of management initiative and the establishment of a more manageable structure with greater decentralisation and accountability.

4.4 Despite this progress, BL is still in crisis. Earlier plans have drifted in key areas. Heavy losses continue and cashflow remains negative. The product range is still weak. Productivity and scale are low in relation to competitors. Business structures and management systems are young and fragile.

4.5 As a result the plans are vulnerable to a wide range of possible perturbations. They assume improvements in market share, resulting from improved efficiency and new products, which may not fully reflect competitors' own advances. A plausible scenario could be one of continuing cash requirements in the quest for viability.

4.6 There are four sets of critical issues currently facing BL. The first is to do with strategy; the second, manageability; the third, vulnerability; and the fourth, privatisation.

4.7 Although different from four years ago, the issues remain large and indicate a continuing leadership requirement of the most substantial kind.

4.8 They also posit the basic requirements for future structure of objectivity, resilience and flexibility.

5 Evaluation of alternatives against the strategic issues

5.1 The strategic questions concern the Company's ability to deliver the Plan and cope with unplanned events. Persistent issues will concern the negotiating posture and limits to be adopted in industrial relations and the attraction of partners to offload fixed costs and secure scale advantages.

5.2 The BL proposal does not claim to improve directly the bottom line. Decentralisation and sharper accountabilities are desirable objectives in their own right and are independent of either corporate structure.

5.3 There is however a set of cost, skill and synergy factors which favour the preservation of a unified structure. Some services are undoubtedly better provided from one centre in terms of cost and quality (tax, legal, treasury, technology and systems). The split into two companies could give rise to some undesired loss of central staffs and disturbance to management systems. These factors are not determinant.

5.4 In terms of strategic direction, the BL proposal makes a general case for the benefits of dedicated Boards totally committed to a narrow range of activities, on the grounds that Cars and Commercial are different businesses.

5.5 The merits of dedicated executive management are self-evident. However, dedicated Boards addressing narrow portfolios run the risk over time of losing objectivity and detachment and the ability to perceive early enough the point at which the underlying assumptions of present strategy have ceased to be valid. Crises demand realistic, stand-back assessment of the widest possible range of options.

5.6 Each company in the BL proposal would be less resilient to any issues such as the closure of Leyland Trucks precisely because of the narrowness of the portfolio. However, structural considerations are less important at the end of the day than the strength of leadership.

5.7 The risk of failing to perceive and grasp a crisis early enough is heightened when the Chairman is part time and Non-Executive. The Chief Executive's perception would be potentially predominant. Particularly in a crisis he may have difficulty in remaining detached and avoiding concern for the wider implications of options, such as closure, for the ongoing rationale of his portfolio and his own future.

5.8 Strategy on industrial relations or collaboration will not be determined by the choice of corporate structure. Both issues are helped by the maximum separation of subsidiary organisational components and of wage bargaining units, which are largely independent of structure.

5.9 In the context of strategic issues, the unified structure is more likely to ensure greater objectivity, flexibility and strength of leadership.

6 Evaluation of alternatives against Manageability

6.1 The issue of manageability is difficult to measure. The problems confronting the Board and the scale and complexity of the business are very large. The Board is of the view that the range of issues is too wide and the incidence of crises too high for a single Board and a single Executive Chairman to handle. Non-Executive Directors commit a substantial amount of time to the affairs of the Company. They argue that the Board, and particularly the Executive Chairman, by virtue of the corporate structure, have a profile which encourages issues to rise to the highest point for resolution.

6.2 They accept on the other hand that many of the major battles have already been fought and ground-rules established for the future. Executive competence is now more broadly based and the preconditions for viability to some extent developed. Nonetheless they feel the need to fragment the leadership task. Their proposal does that by dividing the present position of Executive Chairman across two part time Non-Executive Chairmen. The two Executive Directors become Chief Executives. They already are operating to some extent in that mode and in a unified structure it would be a natural progression to extend the delegation of top leadership further, to reduce the load on a single, highly visible Chairman, without reducing its overall strength.

6.3 The leadership resource envisaged in the BL proposal is considerably less than at present. Two Chairmen each offering a fifth of their time cannot equate with a full time Executive Chairman. The size of the problems confronting the two new Boards can at best be only marginally reduced as a result of the restructuring. The recent Leyland strike has the same dimension whether it occurs in either structure.

6.4 The suggestion that succession will be easier in the proposed structure because the leadership task becomes less onerous is valid only to the extent that the incidence of the problems occurring within each Company will be lower and the risk of spill-over reduced.

6.5 It is not clear how the role of the part time Non-Executive Chairmen of the two new Board will work in practice. The ability of the Chairman, who is ultimately accountable whether non-executive or not, to avoid direct involvement in a crisis is recognised as being extremely difficult. The nature and visibility of the issues which are likely to arise and the need for continuous, sensitive interface with Government will make a part time Non-Executive Chairman's position ambiguous, if not untenable. The intended separation of roles may also force positions of prominence on the Executive Directors for which they are as yet inexperienced.

6.6 On the issue of manageability, the BL proposal is weak because it reduces the quantity of leadership resource and is ambiguous in its definition of leadership roles. This could have serious risks in the handling of a crisis.

7 Evaluation of alternatives against Vulnerability

7.1 The BL proposal attaches great weight to the issue of vulnerability. In a unified structure a crisis in one part of the business exposes other parts to risks in terms of financing, industrial relations, publicity and market confidence.

7.2 In terms of finance a major closure or sale could trigger a renegotiation under duress of the parent company's debt structure and possibly entail the repayment of loans. The BL proposal seeks to reduce those risks by isolating each of the proposed companies from the effects of problems in the other.

The reality of a crisis situation, regardless of corporate structure, would require prompt action including, if necessary, temporary Government guarantees. Such action would mitigate the impact of a crisis on the operational continuity of other parts of the business. Under a unified structure the scale and complexity of a renegotiation would be greater. Under the BL proposal some modest benefit might have been secured through conducting the negotiations outside conditions of duress. However the cost, terms and structure of finance available to the total business, however organised, will be determined primarily by the quantity of assets and quality of earning power of what remains after a crisis, rather than the number of parent companies.

7.3 In terms of industrial relations there is the constant risk that disputes might spread from one part of the company to another. There is little evidence that this has occurred. In fact the degree of insularity achieved has been quite marked.

The risk of cross infection will persist under the BL proposal. The more important means of diminishing vulnerability on the industrial relations front lies in the further decentralisation of authority and structure and, above all, the separation of wage bargaining units. This separation is facilitated by the construction of separate legal entities for the four main parts of the Company introduced on 1st January 1982.

7.4 With regard to the issue of confidence on the part of dealers, customers and suppliers, poor image and high media visibility in a crisis is detrimental to all parts of the Company. The split into two companies may in the long term deflect some of the adverse effects and the search for anonymity of parent company presence will help. However, full resolution of the basic problem of image will depend upon the development of individual images based on the product groups and their commercial success. This can be equally well achieved under either structure.

7.5 On vulnerability, the argument favours the BL proposal, but the balance is marginal.

8 Evaluation of alternatives against Privatisation

8.1 The joint objective of Government and the BL Board is to achieve full privatisation of the Company. BL remains bankrupt against any commercial criteria and the possibility of full privatisation is remote. The possibility of sale to another company on terms acceptable financially and in terms of future employment is also negligible.

8.2 Privatisation options are therefore restricted to disposal of parts of the Company either by flotation or outright sale to a third party. The BL Board is conscious of its responsibility to achieve a 'fair price' and the timing of any disposal will reflect their commercial judgment. Both the Government and the Board are concerned to minimise any negative effects of a disposal on the remainder of the Company.

8.3 Collaboration deals struck to improve the viability of part of the business could subsequently decrease its attractiveness to other parties and thereby impede privatisation. On the other hand, it may also be possible to extend a collaboration arrangement into an equity relationship.

There are no generic interrelationships between privatisation and collaboration; there are only particular cases to be examined on their merits.

8.4 There are no necessary consequences for numbers employed in the event of privatisation by flotation, a precondition of which would be the underlying security of employment. Collaboration deals or disposals to a third party could have significant employment consequences either beneficial or otherwise.

8.5 The privatisation objective requires a structure which is able to respond to specific opportunities as they arise. The narrower the portfolio, the larger the impact of privatisation of a part on the residual structure, and the less its ability to respond flexibly. The proposed split into two companies has this effect.

8.6 Land Rover offers the most realistic opportunity of privatisation over the next two years and an immediate restructuring into two companies could impede this.

8.7 The Chief Executive of the new Commercial company would have understandable difficulty in championing the disposal of the most viable third of its business, particularly if Leyland was failing to perform to Plan. It is also likely to prove difficult to attract a sound management team for the new Commercial company if the objective is to dispose of Land Rover and simultaneously promote the recovery of Leyland.

8.8 Against an objective of early privatisation, the unified structure has a clear balance of advantage.

9 Succession and Continuity

9.1 On the issue of continuity there is substantial value in preserving and building on the hard earned judgment and experience of recent years, and the resolution and unity developed within the present Board. This is most effectively achieved by preserving the present structure. The appointment of a new Chairman might be a significant discontinuity compared with the proposed split into two companies. The disadvantages would be mitigated by the choice of a successor of the highest quality conforming to the emerging leadership profile and supported by the maximum continuity of the present Board.

10 Conclusions

10.1 The immediate options in terms of corporate structure are confined to two - the preservation of a unified structure, containing a number of indpendent business units, or the separation of the present structure into two companies.

10.2 Both options are potentially viable. They have different strengths and weaknesses and carry different consequences, particularly for privatisation and leadership succession.

10.3 The critical issues facing BL remain large. They are to do with strategy, manageability, vulnerability and privatisation.

They indicate a continuing leadership requirement of the most substantial kind. They also posit basic requirements for future structure of objectivity, resilience and flexibility.

10.4 A unified structure has greater qualities of resilience and is more robust in terms of the strategic direction of the business and its manageability.

10.5 Splitting BL into two companies addresses better the issues associated with vulnerability, but perhaps only marginally.

10.6 In terms of privatisation, Land Rover presents the best possibility within the next two years, and a split into two companies now could constitute an impedance.

10.7 The balance of advantage between the two organisational alternatives depends on the weight attached to privatisation and level of confidence of being able to find a suitable successor to Sir Michael Edwardes.

10.8 If high priority is given to early privatisation of Land Rover the unified structure should be preserved at least until this occurs. At that time a principal disadvantage to splitting into two companies would have been removed.

10.9 If it is considered that the right person could be found to succeed Sir Michael Edwardes as Executive Chairman, the case for preserving a unified structure is strong.

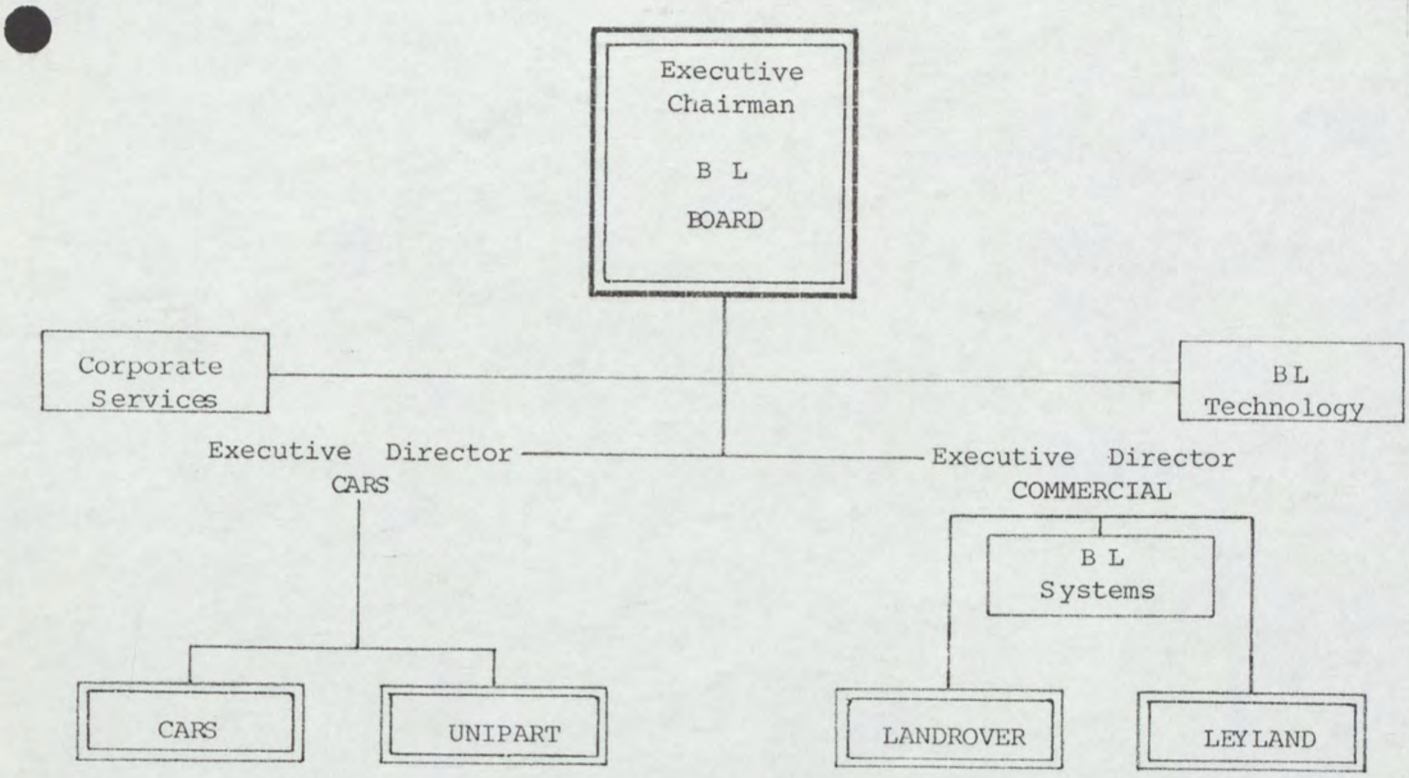
10.10 If privatisation is given lower priority or it is considered that an adequate successor cannot be found then the balance of advantage between the organisational alternatives is substantially reduced.

10.11 An ideal solution could be the retention of a unified structure with Sir Michael Edwardes continuing as Chairman for, say, a further two year period to position the Company for privatisation of Land Rover and the possible subsequent fragmentation into separate corporate entities in the light of the commercial circumstances prevailing. He is in a particularly strong position to achieve the further evolution of the organisation and his stature and knowledge would permit him to perform the role of Chairman on a part-time basis. Such a position would best encourage the greater delegation of corporate leadership to the two Executive Directors in their roles as Chief Executives of their respective parts of the Company.

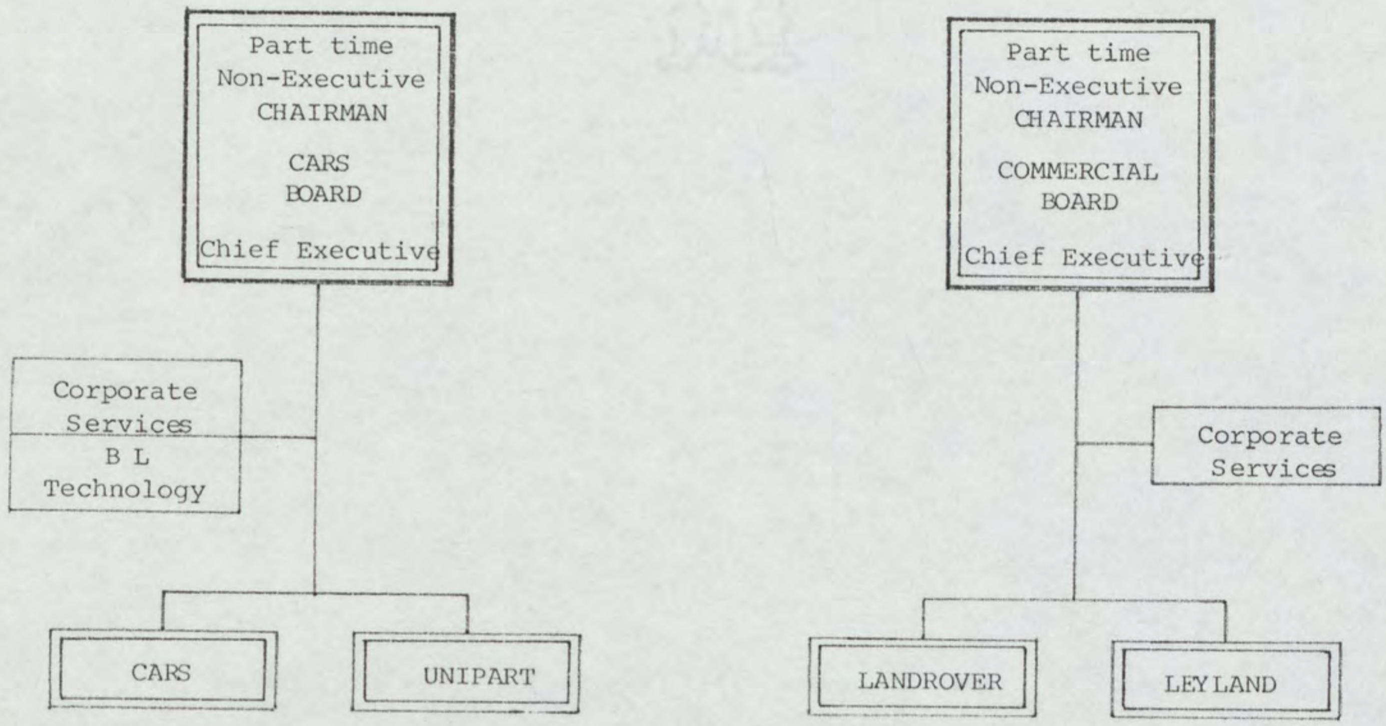
EXHIBIT A

BL ORGANISATION STRUCTURE

EXISTING



PROPOSED



Notes

- The BL Board thinking is that a separate Joint Company, owned equally by Cars and Commercial, would be set up and would contain BL Systems, Nuffield Press and the joint Pension Fund.
- The intention, independent of the Proposal , is to split Cars into separate management and reporting units, Austin-Morris and Jaguar.

EXHIBIT B

THE BL BOARD PROPOSAL

as put forward by the BL Board and agreed with Sir Michael Edwardes on 19.2.82

B.1 The organisation changes proposed are extremely simple. Below the Board they reflect in large measure the present operating structure. There are some complex technical problems associated with implementation, but none are insuperable.

In essence the proposal divides the Company into two free-standing legal entities created around the management structure as it currently exists immediately beneath the BL Board.

One company would comprise Cars and Unipart (Cars); the other Leyland Group and Land Rover (Commercial). Each would have its own Board. The present BL Board would cease to exist.

B.2 The proposal does not change the structure of the four main business components - Cars, Unipart, Land Rover and Leyland - which became legal and management entities in their own right on 1st January 1982.

B.3 The present Corporate Staffs would be broken out across the two new companies. BL Technology would probably be allocated to Cars and BL Systems become part of a Joint Service company.

Inter-group trading affected by the new structure would require a review of existing arms-length arrangements.

B.4 The present BL Board consists of seven directors. The composition of the new Boards remains to be determined, but each would comprise a part time Non-Executive Chairman, three or four Non-Executive Directors and a Chief Executive.

B.5 The intention is to appoint at least one of the two Chairmen from amongst the present Non-Executive Directors and to invite the remaining Non-Executive Directors to join one or other of the new Boards. One or two executives may also join each Board. Additional non-executive appointments will be necessary.

B.6 The situation with regard to individuals is as follows:

The present intention is to invite Sir Austin Bide to be Chairman of Cars.

Sir Robert Hunt is one of a number of possible candidates for the chairmanship of Commercial.

Sir Michael Edwardes has indicated his willingness to serve as a Non-Executive Director on both Boards for a period, if this is thought helpful.

The precise make-up of each Board has not yet been determined.

It is intended to offer the positions of Chief Executive Cars to Mr. Ray Horrocks and Chief Executive Commercial to Mr. David Andrews, before the new structure is announced.

B.7 The proposal deals therefore not simply with structure, but also with the issue of leadership succession to Sir Michael Edwardes at the end of 1982.

EXHIBIT C

BL's RATIONALE FOR THEIR PROPOSAL

as put forward by BL and agreed with Sir Michael Edwardes on 19.2.82

C.1 Vulnerability: The financial and confidence effects of a crisis - or indeed a planned closure or disposal of one component - are better contained if BL is split into two companies.

C.2 Different Businesses: There are no major synergies between Cars and Commercial. They are separate businesses with distinct products, manufacturing processes, markets, customers and distributors. There is, however, important synergy within the cars and commercial vehicle businesses.

C.3 Decentralisation: The proposed structure extends the process of decentralisation and facilitates the splitting out of Land Rover from the Cars pay bargaining unit, which is highly desirable because of the different levels of profitability in each, and is an essential prelude to privatisation. It would limit the effects of the trade union practice of escalating negotiations to the highest level and of seeking the highest common factor in terms of concessions within a single business.

C.4 Dedicated Leadership: Each business would benefit from a more dedicated and focussed Board and management. The proposed structure would eliminate danger of a crisis in one part of the business diverting attention from the strategic problems in another - a problem which resulted in a failure to pick up early enough alarm signals in Trucks, during successive crises in Cars.

C.5 Manageability: The business,in its present stage of recovery,is too complex to be directed by a single Board. The high rate of change experienced in the past will continue and pressures on the top man in particular are reinforced by the high profile and visibility engendered by a single structure. In the proposed structure, four positions will replace those of the present Executive Chairman.

C.6 Image: The disappearance of BL Limited would facilitate the improvement of the image (and consequently of sales) of all its constituent businesses, particularly Land Rover, Leyland and Unipart, by reducing the burden of the "British Leyland" record, which tends to offset the more recent improvements in products, labour relations and productivity.

C.7 Collaboration: Potential partners prefer to deal with businesses which are free standing or not associated with other high risk components. No existing or likely collaborative deal stretches across both businesses. For example, neither BMW or Honda have any interest in being involved with the Truck and Bus business.

C.8 Privatisation: The split into two companies does not impede the pursuit of private sector equity involvement. Indeed private investors will be more easily attracted into the profitable parts of BL if their exposure to risks elsewhere in BL is reduced by the split.

C.9 Continuity: The proposal provides the best possible continuity and corresponds closely to the present management structure. The organisation has evolved with this objective in mind. Therefore experience gained is not dissipated; strategic perspectives and judgments are not broken; and there is a good fit between the executive and non-executive resources available.

C.10 Succession: The proposal removes the need to find a successor to Sir Michael Edwardes and reduces the risk of losing key executives.

EXHIBIT D

RATIONALE FOR PRESERVING A UNIFIED STRUCTURE

D.1 Leadership Succession: The continuing size, complexity and crisis ridden nature of the management task at BL have been brought into focus by Sir Michael Edwardes' impending departure. These demand that the future leadership response is of the highest level possible. The best way of achieving this is to maintain a single Board led by an Executive Chairman of stature, to provide strength and unity of strategic and operational direction, and not to dilute these in any way whatsoever.

The position of part time Non-Executive Chairman for the whole or for part of the company does not measure up to the leadership requirement, is ambiguous and potentially untenable.

D.2 Dedicated Leadership: All businesses benefit from dedicated executives. However, businesses in turbulence and crisis require maximum detachment and the ability of the Board to stand-back and review options. These qualities are best achieved in a 'portfolio' rather than an 'operational' structure. Such a structure minimises commitment and 'ownership' and maximises the ability to confront issues of component viability and sale.

The Board requires the leadership of a full-time Chairman to reduce the risk of being dominated by the Chief Executive.

D.3 Manageability: The problems will remain large and to address them under two structures instead of one will not per se diminish their size but may reduce the range of options for their resolution. Manageability has and will continue to be improved by pursuing decentralisation to discrete business components with maximum autonomy. In addition a wider portfolio permits the retention of high quality corporate staffs essential to the manageability of a decentralised business. Central Staffs would provide a more effective means of coordinating policies which need to be common across the business components than the suggested alternative of cross representation on the two Boards.

EXHIBIT D

(cont.)

D.4 Privatisation: Privatisation requires a structure which provides detachment, resilience and independence of leadership and is able to respond to opportunities as they arise within the widest possible range of options.

The privatisation objective requires a structure which is able to respond to specific opportunities as they arise. The narrower the portfolio, the larger the impact of privatisation of a part on the residual structure, and the less its ability to respond flexibly. The proposed split into two companies has this effect. Land Rover offers the most realistic opportunity of privatisation over the next two years and an immediate restructuring into two companies would be likely to impede this.

D.5 Vulnerability: A crisis situation, regardless of corporate structure, would require prompt action including, if necessary, temporary Government guarantees. Such action would mitigate the impact of a crisis in the operational continuity of other parts of the business. The cost, terms and structure of finance available to the total business however organised after a crisis will be determined primarily by the quantity of assets and quality of earning power of what remains rather than the number of parent companies.

The split into two components is not a condition precedent to the separation of bargaining units within Cars. Separating out into two companies carries the additional risk of the worst situation, in terms of union negotiation becoming the standard for both in the absence of unified direction and control.

D.6 Image: The most effective solution to weak image is the promotion of clear product and marque identities which is independent of corporate structure.

D.7 Decentralisation and Collaboration: These issues are independent of the choice of corporate structure.

EXHIBIT E

FUTURE LEADERSHIP CONFIGURATION

E.1 The key issues confronting the BL Board imply the following configuration of leadership after the departure of Sir Michael Edwardes.

E.2 The overall strategic issue requires above all the ability to assess realistically the condition of the business, in whole and in its parts, and ensure appropriate action by the executive. The personal skills implied are 'helicopter' ability, realism, detachment and the strength to insist.

E.3 Whatever the provenance of a new crisis it will inevitably have implications for industrial relations. The leadership requirement is to assess risk, maintain credibility and locate authority at the right level for the particular situation. The skills required are courage, personal stature and the credibility of a good track record.

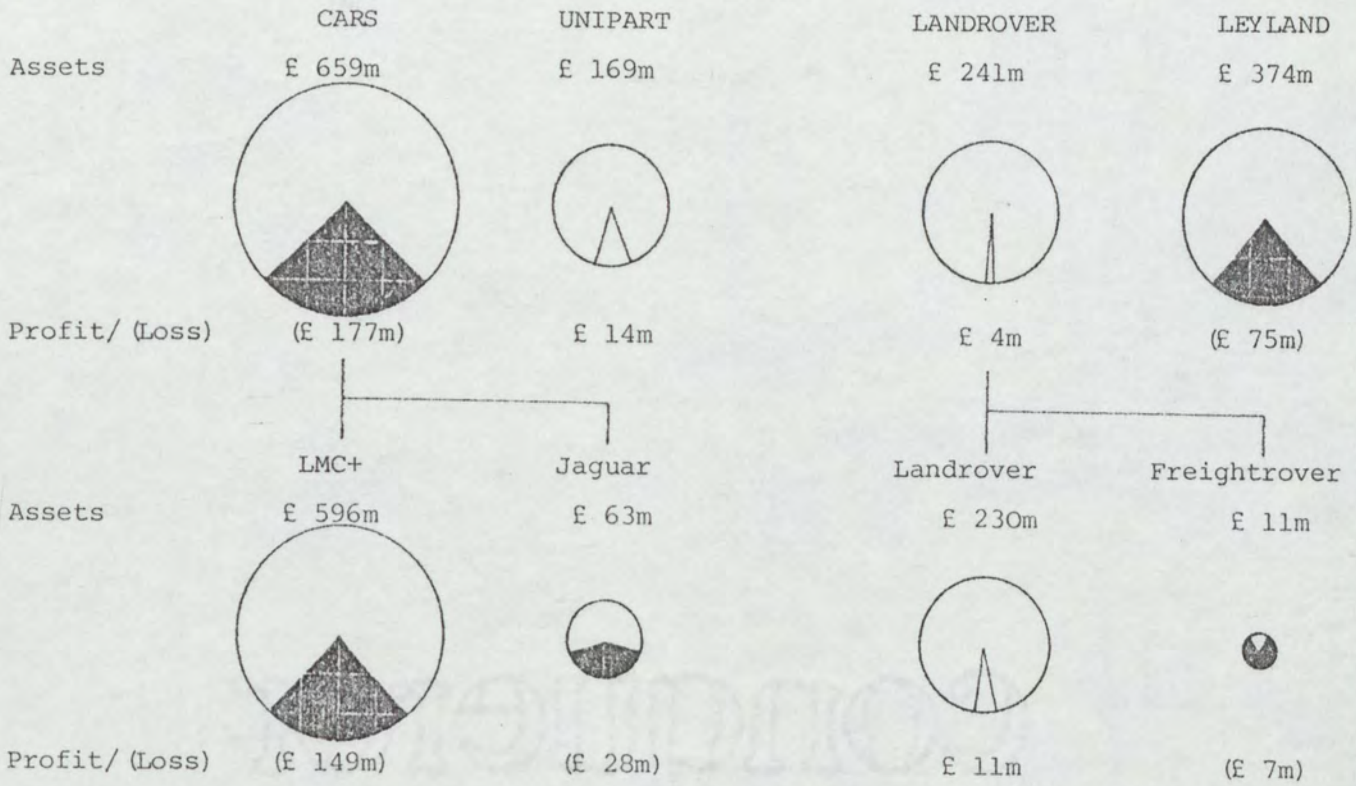
E.4 The construction of a collaboration network requires the entrepreneurial ability to see the opportunity for congruence and mutual benefit between partners; the personality to get the ball rolling and the strength to outweigh the intertia of middle management. The personal skills required are realism, judgment and stamina.

E.5 The privatisation issue requires very fine judgment on matters which go beyond commercial considerations. High public visibility and intense Government interest require sensitive handling of the Government interface.

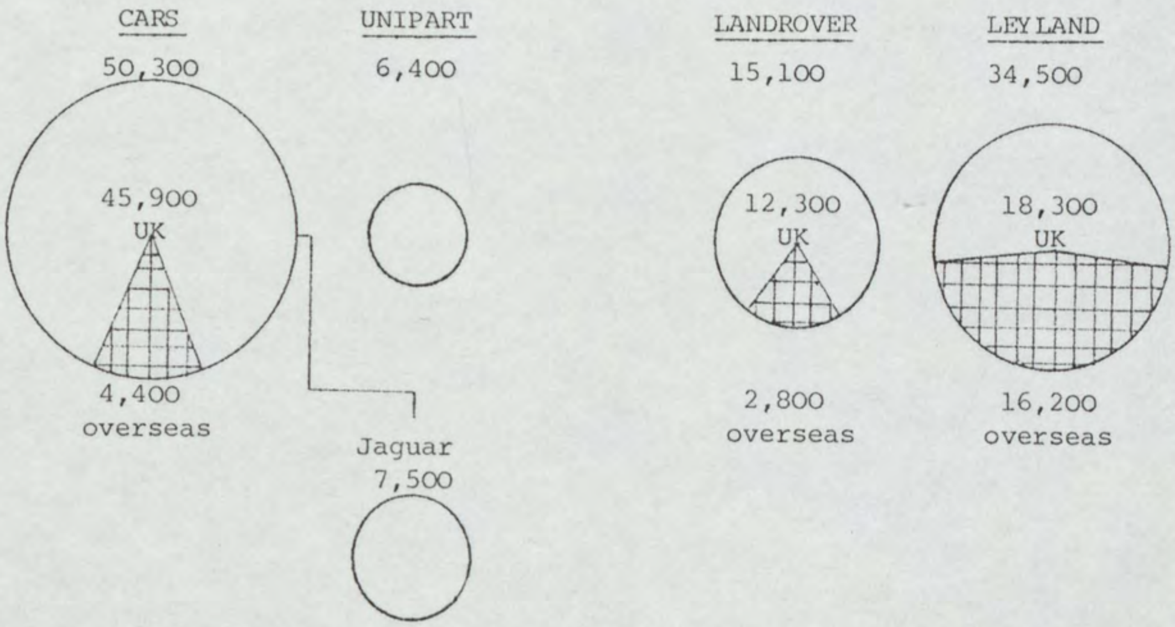
E.6 With regard to manageability, the issues remain large and complex regardless of the particular structure which is adopted. They demand leadership of the highest stature, able to sustain management morale through recurrent crises.

E.7 In terms of background and experience, the leadership requirement is less for a man of the industry than for experience of, structures containing comparable issues of integration and decentralisation.

DISPOSITION & DIMENSIONS OF ASSETS PROFITS & EMPLOYMENT 1981



MANPOWER

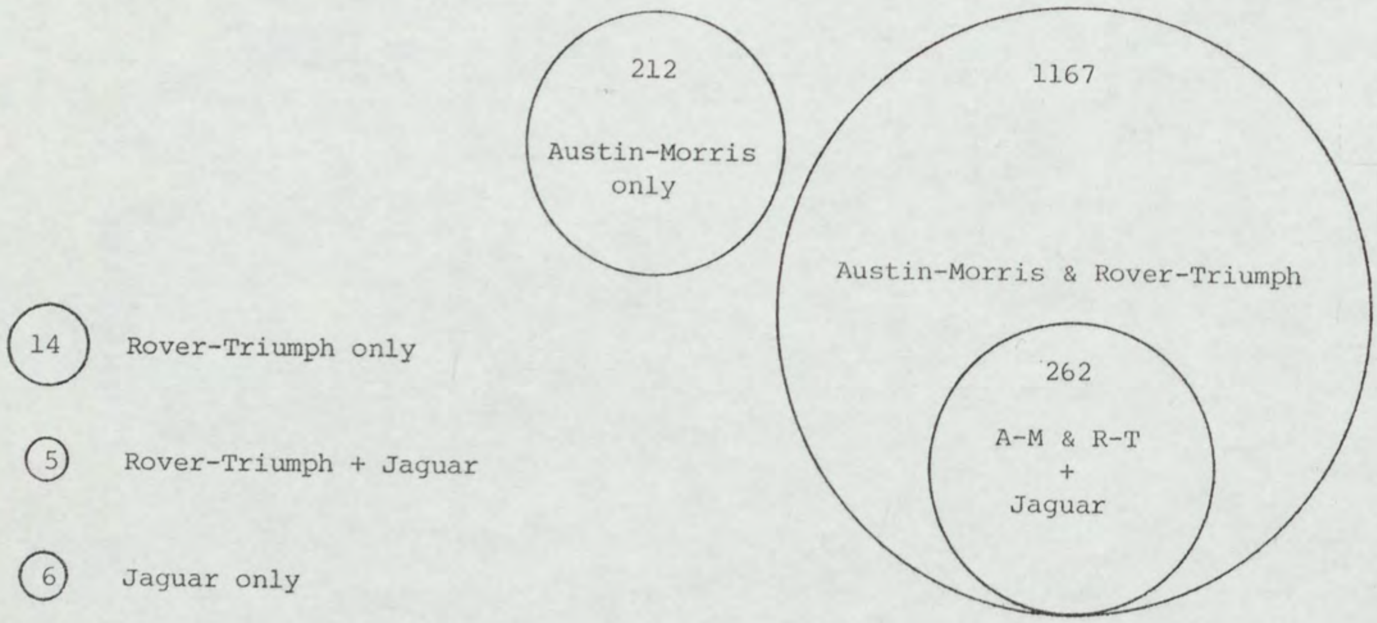


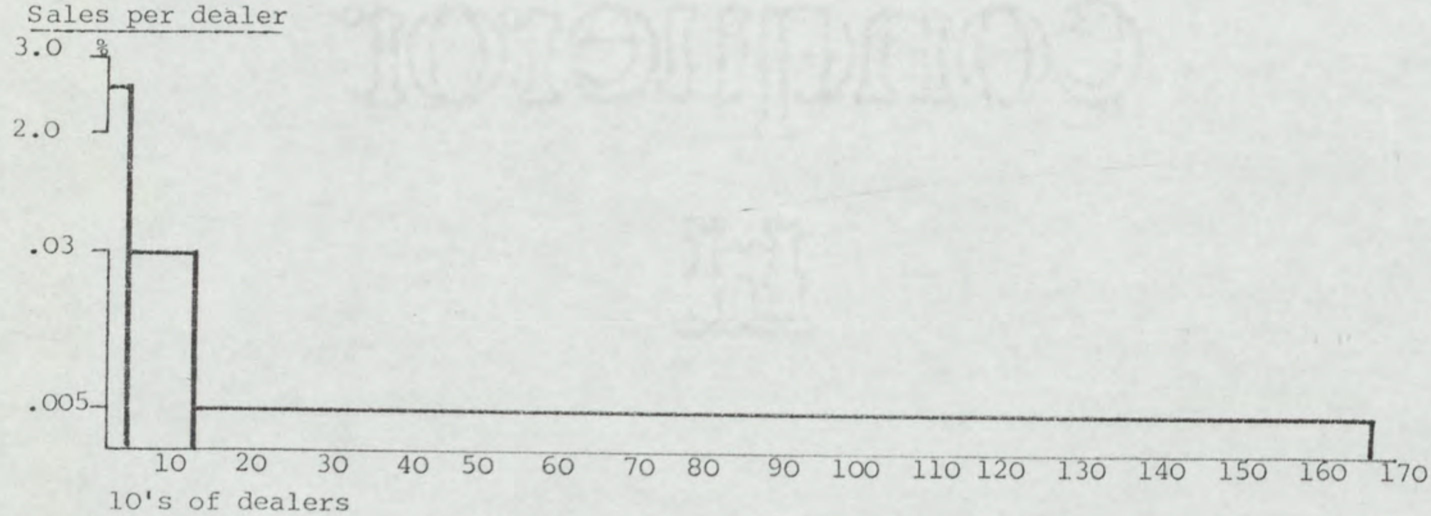
Notes

- All figures from BL Plan 1982.
- Profit/Loss taken before the payment of interest or tax.
- Assets are taken as fixed assets, less depreciation, plus working capital.
- Figures for elements of Groups are derived from ratios quoted in the Plan.
- Separate figures for trucks and buses are not included in the Plan.

EXHIBIT G

MARKETING INTERDEPENDENCIES





- Jaguar It has not been possible to quantify the effects on BL franchise holders in the event of BL ceasing to own Jaguar.Present franchise holders are suffering from low margins and benefit from the higher margins on Jaguar sales.

- Landrover Inter-relationships of UK franchises are not important since only 20% of sales are made in the UK and the large UK sales, eg Ministry of Defence, do not go through dealers. Range Rovers are generally sold in the higher margin end of car franchises.

- Freightrover 300 of the 365 Sherpa franchises are held by Austin-Morris dealers. 80 of the 150 truck dealers also hold Sherpa franchises.

- Overseas Leyland and Landrover are usually interlinked in the assembly overseas of vehicles from kits. The two major subsidiaries, South Africa and Australia, already deal in vehicles from other manufacturers. Any separation of Landrover from Leyland would require similar arms-length arrangements.

MANUFACTURING INTER DEPENDENCIES

CARS	UNIPART	LANDROVER	LEYLAND
Supply of parts →		← Supply of parts	
Jaguar ←			Engine blocks
Side-panels & roof, 2 door →		Range Rover	
Dashboard assembly →		Landrover	
V 8 engine blocks →		Range Rover Landrover	
Axles →		Sherpa	
'O' engines →		Sherpa	
Diesel engines →		Sherpa Freight Rover	
Gearboxes →		Sherpa	
Rover ←		77mm gearbox	
Jaguar (a few) ←		77mm gearbox	
Rover ←		V 8 engine	

SECRET

EXHIBIT I

ARRANGEMENTS FOR COLLABORATION AND OUT-SOURCING

	CARS		LANDROVER		LEYLAND
	L M C	Jaguar	Landrover	Freightrover	
Collaboration	• Honda Acclaim		• Perkins dieselise V8		
Intended Collaboration	• Honda Executive car • Honda Marketing & distribution in Europe	• BMW new model • BMW Joint sourcing of components • Ford Marketing Franchise in Europe		• Alfa-Romeo K2 & MT 210	• ? Replacement L 11 T 11 engin • Cummins/Case Joint manufacture 98 series
Out-sourcing	• VW gearbox LC 10				• R-Royce or Cummins in lieu of L 12/TL 12 engine • International Harvester in lieu some DT 466 engines • Eaton/ZF in lieu Albion gearbox
Intended out-sourcing	• VM diesel • ? transmissions	• VM diesel • BMW diesel ?	• Chrysler automatic gearbox • ZF automatic gearbox	• VW or Salisbury rear axle MT 210	

Notes
- Long standing out-sourcing, eg Borg-Warner automatic gearboxes for cars, not included.
- Intended projects at varied stages.

EXHIBIT J

PRIVATISATION OPTIONS

J.1 Land Rover is not presently self-accounting. Its wage bargaining unit is part of Cars. There are trading interdependencies with Cars, Unipart and Leyland.

The Land Rover Plan projects strong market recovery, maintained market share, a 50% increase in revenue in the two years 1982 and 1983, improving the return on assets to 11%. On this basis a prospectus could just be contemplated 18 months from now. It would presuppose self-sufficiency as a business unit and trading interdependencies being placed on a secure commercial footing.

Land Rover could probably be sold to another Company earlier than this. A partial sale would also be attractive to potential collaborative partners. Such a move could impede subsequent disposal or flotation of the whole.

Exclusion of Freight Rover which is currently in the early stages of recovery would marginally enhance the prospects of sale or flotation.

J.2 On the Plan projections full privatisation of Leyland is very unlikely before 1984/5. Prospects for early outright sale of the whole, given the depressed state of the industry internationally, are only marginally higher.

It would be possible to sell some of its business components, such as Scammel, overseas companies and Bus in the event of an abandonment of the 1982 Plan and closure of the main UK Truck manufacturing activity.

J.3 Jaguar is extremely fragile and its performance precludes it becoming a free standing business through flotation for the foreseeable future. Its volume throughput is very small by the standards of the industry, and new models require substantial investment. It is planned to be cash consuming until 1984.

Despite its vulnerability, the marque has high continuing prestige and the business might be saleable to another cars company either in one move or through progressive collaboration and equity investment, for example with BMW.

EXHIBIT J

(cont.)

J.4 Unipart is a service business and integral to Cars and could only become a free standing business in the event of liquidation of cars when it would have residual value as a declining business.

Partial sale through flotation or placing with investors would be possible subject to its commercial viability and trading arrangements satisfying independent scrutiny. This would introduce inflexibility in spare parts pricing and thereby reduce the attractiveness of the Cars business to a potential purchaser.

J.5 The cash flow of Volume Cars including Unipart remains strongly negative for the next two years precluding any possibility of sale by flotation. Privatisation could only arise as part of a collaborative venture, which created a high degree of interdependency with another group aimed at securing viability through economies of scale. The relationship with Honda could develop in this way.

EXHIBIT J

(cont.)

PRIVATISATION OPTIONS

The table below sets out the principal privatisation possibilities, assuming achievement of the 1982 Plan.

	Net Assets (1) 31.12.81	Planned Net Cash Flow (2) 1982 and 1983	Full Sale within 2 years (3)		Partial Sale within 2 years (4)	
			By Public Flotation	To a Third Party	To financial investors	To collaborative partners
	£m	£m				
Land Rover	241	5	Medium	High	Medium	High
Leyland	374	(61)	Nil	Low	Low	Medium
Jaguar	63	(51)	Nil	Low	Nil	High
Unipart	169	26	n.a.	n.a.	High	Low
Volume Cars and Unipart	828	(177)	Nil	Nil	Nil	Medium
BL	1518	(591)	Nil	Nil	Nil	Low

Notes:

(1) Net Assets at 31.12.81 are taken from the 1982 Plan and are defined as fixed assets less depreciation plus working capital before deducting borrowings.

(2) Net Cash Flow for the two years 1982 and 1983 is defined as profits before interest and tax, plus depreciation, less capital expenditure, and less working capital increases.

(3) Full sale is defined as a disposal sufficient to ensure that total management and financial responsibility, subject to implementation of transitional commitments in the terms of sale, passes to the new owner.

(4) Partial sale is defined as a disposal under which the seller retains effective management and financial responsibility. In the case of public flotation the seller's equity might be reduced to under 50% but would remain in excess of 30%.

EXHIBIT K

TERMS OF REFERENCE FOR THE CONSULTANTS

1. To consider and make recommendations in the light of the draft Government objectives for the group (copy attached), on whether any changes are desirable, in connection with the departure of Sir Michael Edwardes at the end of 1982 in the organisation for management of the activities within the BL group, and if so what form of organisation might best meet these objectives.

2. The investigation will evaluate the proposals made by Sir Michael Edwardes and the Board and recommend alternatives where appropriate; taking into account (i) the Government's need as shareholder to satisfy itself that any changes will not prejudice the objective of returning the businesses to the private sector; (ii) the Board's responsibilities (a) to make commercial judgments and (b) to measure and control the operating efficiency of the company.

The study should cover the possibility of retaining a single holding company with two or more major operations, or a number of smaller operations, for which management responsibility is fully delegated.

3. This assignment should be completed within four weeks. All contacts with BL should be made through the Chairman. In view of the commercial confidentiality of this enquiry, no contacts should be made with organisations other than BL and the relevant Government departments without prior consultation with the Chairman.

EXHIBIT K

(cont.)

DRAFT OBJECTIVES

The objectives for BL's business are:

1. To plan and implement the strategy approved in the 1982 Corporate Plan for the return of all the constituent businesses, either together or separately, as soon as practicable, to the private sector, and to ensure that nothing done under 2 or 3 will prejudice this strategy.

2. Consistent with 1, to dispose of or close peripheral activities so as to concentrate on vehicle manufacture and sales.

3. To pursue a programme of product, market and business development, wholly within the limits of public funding already agreed for the financial years 1981/2 and 1982/3 and announced by the Government, so that the business can be made to operate on a continuing commercial basis, and in particular to bring about the achievement of a rate of return sufficient to attract external funds on normal commercial terms to enable the business to trade independently of Government support.

EXHIBIT L

SCHEDULE OF MEETINGS

January

27th J.R. Ibbs, Head, Central Policy Review Staff
G. Mackenzie, Central Policy Review Staff

28th P. Jenkin, Secretary of State for Industry
N. Lamont, Minister of State, Department of Industry
G. Manzie, Deputy Secretary, Department of Industry
J.R. Ibbs
G. Mackenzie

Sir Michael Edwardes, Chairman, BL
B.T. Wilson, Director of Organisation and Personnel Planning, BL
R. Holmes, Personal Assistant to the Chairman, BL
J.R. Ibbs
G. Mackenzie

29th B. Mountfield, Under Secretary, Department of Industry
J. Bowder, Assistant Secretary, Department of Industry

February

1st G. Manzie

2nd F.L. Fitzpatrick, Director of Finance, BL

N.J. Carver, Director of Business Strategy, BL

3rd A.R.W. Large, Company Secretary, BL

B.T. Wilson, BL

4th J.W. McKay, Director of Communications, BL

D.R.G. Andrews, Executive Director, Leyland & Land Rover Groups, BL

5th G. Mackenzie
C. Beauman, Central Policy Review Staff

J.R. Ibbs

8th Sir Peter Carey, Permanent Secretary, Department of Industry

R. Horrocks, Executive Director, Cars & Unipart, BL

9th W. Ryrie, Second Permanent Secretary, The Treasury
A. Lovell, Under Secretary, The Treasury

10th Group Meeting with BL Non-Executive Directors

Sir Austin Bide, Non-Executive Director, BL

11th	J.R. Mayhew-Sanders, Non-Executive Director, BL
	Sir Michael Edwardes
	Sir Robert Clark, Non-Executive Director, BL
12th	J.R. Ibbs
18th	Sir Robert Hunt, Non-Executive Director, BL
19th	Sir Michael Edwardes
22nd	R.E.B. Lloyd, Deputy Chairman, Hill Samuel J.A. Leek, Director, Hill Samuel
23rd	R. Mountfield J. Bowder
	Sir Peter Carey
24th	J.R. Ibbs
	Sir Peter Carey

Mr. R. Holmes, Personal Assistant to the Chairman of BL, was present at all BL meetings including those with the Non-Executive Directors and was also at the meeting with the Hill Samuel Directors.

In accordance with the agreed terms of reference we asked Sir Michael Edwardes if we could see Mr. I. MacGregor, Mr. A. Frost and Mr. P. Lowry, all former Directors of BL, and he preferred that we did not.