



PRIME MINISTER

British Airways Privatisation and US Anti-Trust Suits
(MISC 112(85)2, 3, 4, 5 and 6)

BACKGROUND

You chaired a meeting on 17 December on British Airways (BA) privatisation and anti-trust suits. Since then, the postponement of the privatisation of BA has been announced; and Mr Ridley has obtained agreement in correspondence (his letter of 15 January) to a settlement of the civil action with the Laker liquidator if available on terms close to those in Annex A to his paper MISC 112(85)2. That paper and MISC 112(85)5 by the Financial Secretary, Treasury consider the next steps on the remaining United States (US) class anti-trust actions, their relationship to the privatisation of BA and future dealings with the United States Government on anti-trust and the Bermuda 2 agreement. MISC 112(85)6 gives the views of the Foreign and Commonwealth Secretary. MISC 112(85)3 and 4 by the Secretary of State for Transport explore in further detail some matters incidental to the main issues.

MAIN ISSUES

2. The main issues are:
 - i. what are the prospects for a settlement of the liquidator's action?
 - ii. How should BA proceed in relation to the class actions and what are the implications for privatisation?
 - iii. What further action should be taken and when to seek changes in US policy and/or legislation on



Bermuda 2 and the anti-trust laws?

The Liquidator's Case

3. You will want to hear the latest prospects for a settlement from Mr Ridley. His suggestions in paragraphs 15 and 16 and Annex II of MISC 112(85)2 about presentation have been generally accepted subject to comments made in correspondence, but it may be worth considering

- i. can the Government, as 100 per cent shareholder in BA, maintain the complete detachment from the Board's decisions to settle proposed by Mr Ridley?
- ii. Can Mr Ridley be reasonably confident that the Comptroller and Auditor General will respect BA's wish to keep the terms of the settlement secret?
What might the implications be if he did not?

Anti-Trust, Bermuda 2 and Privatisation

4. Assuming that the liquidator's suit is settled, Mr Moore does not at this stage take issue with Mr Ridley's view that tactics in the next phase should be to try for an early settlement of the class actions if there is a real chance of one. BA is getting further advice bearing on this.

5. If it is not clear within a week or two what the chances are, however, Mr Ridley's and Mr Moore's views diverge. Mr Moore favours making privatisation the priority and giving a partial indemnity to allow it to proceed quickly. Problems with the US on Bermuda 2 and anti-trust should be pursued in parallel, but might have to be lived with. Mr Ridley seems prepared to wait longer for prospects in the class actions to clarify and would oppose on cost grounds an indemnity of the kind suggested by Mr Moore. He would give priority to negotiations with the US on Bermuda 2 and anti-trust, possibly including, if necessary,



notice of withdrawal from Bermuda 2; and/or what he sees as the less extreme possibility of a compensation fund financed by a ticket tax of the kind discussed in MISC 112(85)4.

6. Under Mr Ridley's proposals, privatisation would clearly take a good deal longer than under Mr Moore's, though he says he hopes it could be achieved in 1985/86. He does not appear to rule out the possibility that, in the long run, privatisation might go ahead before the class suits and negotiations with the US were over, but he proposes to choose a new target date only once decisions have been taken on

i. whether or not to threaten withdrawal from Bermuda 2 (presumably because this would have particularly major implications for the privatisation prospectus); and

ii. airports policy (on which he is due to make proposals in the next 2-3 months).

7. The Foreign and Commonwealth Secretary agrees with the Financial Secretary that the prime objective should be to neutralise the effects of anti-trust actions arising from the past. That apart, he neither supports nor rules out either Mr Moore's or Mr Ridley's approach unequivocally.

An Indemnity

8. The advantage of a partial indemnity (ie. with the Government bearing any costs in excess of some threshold amount - say \$30-50 million which would remain the responsibility of BA) would be that it might allow privatisation to proceed. (The alternative option of separating BA plc from its anti-trust liabilities, discussed in MISC 112(85)3, is no longer being contemplated by the Treasury.) The disadvantages are that it would weaken BA's incentive to secure a tolerable outcome of the actions and would whet the appetite of the

but not
eliminate



litigants. It would of itself increase the likely cost of resolving the suits, which might, at worst, be very significant compared with the proceeds of privatisation. The extent of the possible financial exposure is not entirely clear, but Mr Ridley mentions a theoretical maximum of \$1 billion; an amount exceeding \$100 million cannot be ruled out at this stage. The nature of the risk would have to be admitted at the time of privatisation and could well provide severe public and Parliamentary criticism.

Pressure on the US

9. Both Mr Moore's and Mr Ridley's approaches would have implications for relations with the US. The former could be seen as in effect accepting the application of the US anti-trust law to air services covered by the inter-Governmental agreement, since going ahead soon with privatisation would not be compatible with determined pressure on the US for a change in the situation - the action open to HMG (eg. withdrawal from the Bermuda 2 Agreement) could have a major impact on airline profitability, to which reference would have to be made in the prospectus. On the other hand, Mr Ridley's approach of political confrontation - whether through ending the Agreement or through the threat of a ticket tax - could have unpredictable and far-reaching consequences, which would require much further evaluation. A meeting under the Foreign Secretary on 6 December ruled out an indemnity in respect of the liquidator's action and expressed serious reservations about a ticket tax or other means of raising the political profile of the dispute. It may be worth pressing his representative (Mr Renton) on what course of action he would prefer if an early settlement of the class litigation seemed impossible.

Public Presentation

10. The difficulties of presenting any form of indemnity in relation to privatisation are touched on in paragraph 8 above. More generally, there would be difficulty in getting



over to public opinion why, if by reason of international agreement, US domestic anti-trust law ought not to apply to BA, it was necessary for the UK Government to pay for breaches by BA of that law rather than seek redress through legal and diplomatic channels. Moreover, Mr Ridley's compensation fund scheme, though it would remove or reduce the cost to the taxpayer of indemnifying BA, would increase costs to travellers, who are already seen in consumer circles as losers from alleged action by BA and other airlines in the Laker affair.

Next Steps

11. There are two keys to early progress. The first is a settlement with the liquidator. If that falls through, there will need to be a review of the consequences - which could be severe - for early privatisation of BA and for the Government's financial exposure if any indemnity were given. The second is the further information to be available 'in a week or two' on the prospects of an early settlement of the class actions. The Group will need to meet again to decide, in the light of this information, whether to pursue a settlement or one of the alternatives proposed by Mr Ridley and Mr Moore. It will, however, be possible now to establish whether there is any preliminary consensus on which alternative is preferable.

12. Additional work for a further meeting of the Group might be helpful on the following matters in addition to the prospects for the settlement of the class actions:

- i. what are the best assessments of both theoretical and likely actual exposure of BA and the Government under a partial indemnity of the kind contemplated in MISC 112(85)5?
- ii. In Mr Ridley's judgement, what is at risk in economic terms if the present Bermuda 2/anti-trust situation is allowed to continue? If the situation could be shown to inflict significant economic loss on the UK, and if there were a realistic prospect



that we could mount effective pressures on the US for a change, then there would be an argument for tackling that problem before going ahead with privatisation.

iii. What would be the options for the public presentation of the indemnity proposed by Mr Moore and the compensation scheme suggested by Mr Ridley; and what would be the likely public reaction -

- a. in the UK; and
- b. in the US?

13. If the Group does not rule out Mr Ridley's idea of a ticket tax, there seems no reason why the further work he suggests on it should not be done, though the suggestion that legislation should be prepared on a contingency basis seems premature.

HANDLING

14. You will want to invite Mr Ridley, Mr Moore and Mr Renton to speak on the Government's objectives and next steps. All other members of the Group will wish to contribute: you will wish to record their preliminary views on the alternative approaches suggested by Mr Ridley and Mr Moore.

CONCLUSIONS

15. You will wish to reach conclusions on the following:

- i. a settlement of the liquidator's actions;
- ii. with a view to a resumed discussion, further work -
 - a. by the Department of Transport to clarify the prospects for an early settlement of the class actions;
 - b. by the Department of Transport and the Treasury on the matters at paragraphs 12(i) to (iii) above.

PLG
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