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PRIME MINISTER

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SHARES FOR EMPLOYEES

In his minute to you of 13th March Keith Joseph reported on the deadlock which had been reached in his E(DL) Sub-Committee on the arrangements for an employee shareholding scheme on flotation of BAe. The issue - whether there should be a free offer of shares to all qualifying employees - was never resolved because the immediate urgency evaporated, with the decision to postpone the BAe flotation. We agree that in the Lords Debate on the BAe Bill, the Government spokesman should take a holding line.

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2. In a letter to me of 6th May, John Nott has now raised the question of what should be said about employee shareholding during the later stages of the Civil Aviation Bill. He too wants to announce a free share issue to employees, combined with a "one for one" offer. I have therefore been considering what our general approach should be in the light of the specific proposals from Adam Butler and John Nott, the earlier E(DL) discussions and the changes in the current Finance Bill. There are a number of considerations. First, we want arrangements which are a practical demonstration of our aim of encouraging wider share ownership, especially among employees. But there are significant differences between the corporations which we propose to float in terms of attractiveness to the market, number of employees, likely net disposal proceeds. We cannot therefore have entirely uniform arrangements. On the other hand we need enough consistency

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of treatment to avoid any differences giving a lever to those within the industries opposing privatisation. Second, the arrangements must be secured at a cost to the Exchequer which is reasonable in terms of preserving the benefits to the PSBR of flotation.

3. To meet these points, I suggest that our general approach should be to set a cash ceiling on the amount of the disposal proceeds to be devoted to encouraging employee shareholding, equivalent to 4 per cent of the expected gross proceeds. Where 50 per cent of the equity is to be sold, this should buy a minimum 2 per cent employee shareholding and this figure could be increased reflecting on the distribution between free offers and one for one schemes. It is essentially Adam Butler's original proposal for BAe and would cover John Nott's recent proposals, although with the imposition of a cash ceiling. I believe that a monetary limit other than the limit of £1,000 under the Finance Bill is necessary. Without it we risk a considerable part of the disposal proceeds being swallowed up, especially where employee numbers are large in relation to the expected value of the equity.

4. Within the cash figure the precise balance between free offers and one for one offers would lie with the sponsor Ministers concerned. They would want to take account of the likely impact of each in the particular circumstances of each industry, although there would be an incentive for one for one schemes to maximise employee shareholding within the ceiling. However, I think we must accept that any free offer will set a precedent which will be difficult to avoid in subsequent cases. To avoid the costs of these offers escalating, we must therefore confine

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them to £50 a head, even in cases where a much higher figure would be consistent with the 4 per cent ceiling. The fairness of our treatment of individual cases is likely to be judged on this point.

5. Finally there is the question of the timing of setting the ceiling. The merchant bank's estimate of market capitalisation may change significantly in the period before flotation. This is especially relevant in the BA case where John Nott wants agreement to his scheme now in order to announce it during the later stages of the Civil Aviation Bill, although flotation is not expected before 1981 at the earliest. We can of course agree on a rough figure now, related to the latest estimate of market capitalisation, but I think we should agree a final figure only at the point at which we give the go ahead to flotation, having satisfied ourselves that the expected yield is acceptable.

6. I am copying this minute to Keith Joseph, other members of E(DL), Norman Fowler and Sir Robert Armstrong.

A handwritten signature in dark ink, appearing to be 'G.H.' with a flourish.

(G.H.)

18 June, 1980

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