



10 DOWNING STREET

*From the Private Secretary*

7 December 1981

THE BRITISH ALUMINIUM COMPANY, LTD

I attach a copy of a letter the Prime Minister has received from Lord Plowden about the Invergordon smelter. I should be grateful for a draft reply for the Prime Minister's signature. It would be helpful if this could reach me by Monday 14 December.

The Prime Minister, who was warned in advance that Lord Plowden was likely to write, has indicated that she is ready to see Lord Plowden.

I am sending a copy of this letter, and its enclosure, to John Kerr (H.M. Treasury), Richard Dykes (Department of Employment) and Muir Russell (Scottish Office).

M. C. SCHOLAR

I. K. C. Ellison, Esq.,  
Department of Industry.



*filed*

10 DOWNING STREET

*From the Private Secretary*

7 December 1981

I am writing on behalf of the Prime Minister to thank you for your letter of 7 December, about Invergordon.

I will place this before the Prime Minister at the earliest opportunity, and a reply will be sent to you as soon as possible.

M. C. SCHOLAR

The Lord Plowden, K.C.B., K.B.E.



# BACO

## The British Aluminium Company Ltd

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The Rt Hon Margaret Thatcher MP  
10 Downing Street  
LONDON SW1

Your ref

Our ref

*I am Prime Minister*

Prime Minister

(2)

*I'm not sure if you saw this  
in last night's box. I have asked*

FROM THE LORD PLOWDEN KCB, KBE

*A need  
not*

*ready to see Lord Plowden.*

*E(EA) is discussing*

*tomorrow; then you will  
be consulted. See, too, Mr Younger's*

*MCS 8/12*

*paper.*

Date

7 December 1981

*cc Mr D Wright (Co)*

THE BRITISH ALUMINIUM COMPANY, LTD

I am writing to you in my capacity as a past Chairman of The British Aluminium Company and of the parent company, Tube Investments Ltd (of which I am now President,) and as one who was personally involved in the negotiations between BA and the Government concerning the building of the Invergordon smelter. I hesitate to trouble you when you have so many preoccupations, but the decisions which are about to be taken are of the greatest possible significance for the future of BA. Moreover they do, I believe, raise important points of principle about relations between government and industry.

As you may know, BA's Invergordon smelter is in severe financial difficulty. Because of disproportionate escalation in power prices the plant has become totally uneconomic, and losses have reached a level where they threaten to destroy the whole BA Group. BA has been discussing the problem with the Department of Industry and the other departments principally concerned. Because BA is locked into the Invergordon project by the nature of its agreements with the Government and its agencies, it can only resolve its difficulties with their consent and co-operation.

BA would not be involved in Invergordon but for the enthusiasm of the Government of the day for setting up a primary aluminium industry in the UK. The company proceeded with the project on the basis of advice and assurances of the Government and its agencies, principally with regard to power costs. I can categorically state I would not have allowed BA to proceed with the proposal without Edmund Dell's formal letter of 23 July 1968, written when he was Minister of State at the Board of Trade (the key sections are marked on the second page of the copy attached.)

BA has fulfilled all its undertakings. Invergordon has become totally uneconomic because the assurances given to BA have not been fulfilled.

- 1 BA built Invergordon on schedule and within 1968 budget costs.
- 2 Power costs from Hunterston B were expected to keep Invergordon competitive with smelters based on hydro-electric power. Hunterston B was four years late, cost 40% more than the 1968



estimate, and capacity is now only 80% of design. In 1981 Hunterston B operating costs charged to Invergordon are nearly 13 times the 1968 estimate, compared with approximately 4½ times for the smelter's other production costs and for general inflation.

The company's financial problems have been further compounded by the uncertainties of a £44 million court case directly related to power charges. BA's legal advisers believe that the company is not liable for the disputed items, some of which relate to estimated costs which have not yet been incurred, but BA does not have the financial resources to await the outcome of legal process to prove its case.

In 1981 the Invergordon smelter will lose £20 million. BA cannot sustain such a rate of loss or the uncertainties arising from the dispute with the Electricity Board. In the absence of a reasonable and speedy settlement, the Board of BA is faced with the immediate prospect of putting the whole Group into liquidation.

Against this background, BA has decided that it has no choice other than to close the smelter and to seek cancellation of the agreements and the termination of the financial arrangements on which the whole undertaking was based. The basis of termination will decide the future of the rest of the Group.

Although the electricity charges currently made to Invergordon have turned out to be uneconomic for aluminium smelting, they are still a good deal lower than the cheapest tariff available to other industrial consumers. Consequently, the electricity released to the system by the closure of Invergordon will mean major financial benefits for the Electricity Boards.

Under the 1968 power contract which runs to the year 2000, BA is entitled to a payment equivalent to those benefits - or in the language of the contract - the "residual value." If BA were to take the matter to court it could well obtain a very substantial sum for its shareholders, amounting to several hundreds of millions of pounds. Unfortunately, from BA's point of view the time required for litigation does not make this a practical possibility because of BA's financial position. However there is no doubt that if BA were forced into liquidation the liquidator would be obliged to pursue the matter in the courts.

I believe that a fair settlement of this most difficult problem should take account of the "residual value" of the power contract and of the assurances given to BA in 1968. I understand that there is broad agreement between departments that a settlement arising from the "residual value" clause should encompass writing off the loan from the Board of Trade which enabled BA to contribute to the capital cost of Hunterston B, and the cancellation of the disputed charges mentioned above. A settlement which went no further than this would leave BA in a dangerously weak financial position and would force the company to close down other UK plants which it believes are capable of being competitive when current efficiency improvements have been completed.

Although I am all too conscious of the public expenditure constraints, I feel that a fair settlement really has to include a measure of cash. BA would regard a net payment of £30 million as at least enabling it to stand the Invergordon closure costs and the write-off of fixed assets without irretrievably damaging the rest of the business. Such a figure is still encompassed well within the claim BA would have under the "residual value" clause and would in no way compensate BA for the losses incurred as a result of its involvement in the project. As it is, Invergordon has resulted in direct losses for BA of £63 million and indirect losses substantially in excess of this figure, including, for example, giving up a major asset in Canada to finance the building of the Invergordon smelter.



It is perhaps relevant to point out in this context that the position of the Anglesey smelter has been quite different. Although I was given an assurance that the arrangements with Anglesey were in all essential respects the same as those for BA, it is known that Anglesey has in fact been getting its power substantially cheaper than BA, and I understand that they have been making reasonable profits.

BA is not a lame duck. Even with the burden of Invergordon, its track record compares favourably with its UK and European competitors. Without Invergordon it will be a viable company - provided that its short-term policies are not distorted by the pressures of high gearing caused by the damage inflicted by Invergordon and too parsimonious a settlement.

The time-scale is short. At present the company is unable to produce a balance sheet as a going concern, and the year end will demand a full exposure of its problems. In these circumstances, I should be most grateful if I might come to see you accompanied by Mr Ronny Utiger, the Chairman of BA, before any final decisions are taken.

Yours sincerely

Edwin R. P. Rowland.





From the  
Minister of State

BOARD OF TRADE  
1 VICTORIA STREET  
LONDON S.W.1  
ABBEY 7677

22 July, 1968

*Dear Sir William,*

I am writing with reference to various matters we have discussed in connection with British Aluminium's projected reduction plant at Invergordon.

#### Power Contract

You have shown me the Heads of Agreement for the project signed between the North of Scotland Hydro Electric Board and the British Aluminium Company Limited, dated 22nd July, 1968, which provides for the company to make a capital contribution to NOSHEB in connection with the supply of electricity required for a period of 29 years for a reduction plant rated at 100,000 tons annual output of aluminium. The Heads of Agreement provide for a capital contribution currently estimated to be £25.8 million, representing the capital cost of transmission and 20 per cent of the capital cost of Hunterston B.

#### Government Loan

... I attach a copy of a Memorandum setting out the main points which we have agreed should be included in a loan agreement between the Board of Trade and the British Aluminium Company Limited. This Memorandum outlines the terms of a Government loan to cover B.A. Co.'s actual contribution to NOSHEB. I confirm that it is the Government's intention to seek the approval of Parliament, in the next session, for an industrial investment scheme under the Industrial Expansion Act, 1968, which will authorise the making of the Board of Trade loan.

#### Plutonium Purchase

I note that, under the Heads of Agreement with NOSHEB, B.A. Co. have the right to transfer as plutonium nitrate to the Ministry of Technology 20 per cent of the plutonium calculated to have been produced in the reactors at Hunterston B. The Government have agreed that the Minister of Technology will enter into a contract with the British Aluminium Company Limited whereby (subject to the approval of Parliament to the necessary expenditure), B.A. Co. will transfer the right to this plutonium nitrate to the Minister in consideration of which the

/Minister

Sir William Strath, K.C.B.,  
British Aluminium Company Limited,  
Norfolk House,  
St. James's Street,  
London, S.W.1.





Minister will make quarterly payments to B.A. Co. of £30,250, commencing on 15th May, 1971, until the NOSHEB supply agreement is terminated. This figure of £30,250 will be adjusted to take account of any changes in the estimated quantities of plutonium resulting from any changes in the share of Hunterston B in respect of which B.A. Co. has made a capital contribution to NOSHEB. There will have to be some provision for retrospective adjustments in the event of the Power Agreement's being terminated in its early years as a result of an act or default by B.A. Co.

#### Capacity of the reduction plant

The Board will be glad to review the situation with you if you wish to increase the plant's capacity when market and other conditions permit, so that there can be full consideration of all the likely effects of your plans, and in particular the ways in which the additional capacity might be achieved. In this connection, you are aware that the British Government have told our EFTA partners that we propose to review with the aluminium companies, not later than 1971, the further expansion of smelters in the United Kingdom so that there may be full consideration of the likely effects on Norwegian interests before decisions are taken. I have taken note of your assurance that B.A. Co. will not, before this date, decide to extend its capacity at Invergordon above 100,000 tons without prior consultation with the Government.

#### Capital and running costs of Power Station

In assessing the commercial viability of an aluminium smelter on the power terms and loan arrangements offered to you, you expressed great concern that the escalation on capital and running costs for power might operate so unfavourably as to make the effective power price uneconomic. You were given opportunities to obtain the views of the Atomic Energy Authority, the South of Scotland Electricity Board and the North of Scotland Hydro Electric Board on the probable future course of capital and running costs. The extent of escalation envisaged by these bodies was relatively small and fell within the limits which you judged to be tolerable. I recognise that in agreeing to proceed with an aluminium smelter at Invergordon you have given considerable weight to these views, put forward in good faith, and accepted by you as such.

#### Review

We agree that the Board of Trade and the British Aluminium Company Limited will consult together if circumstances arise which, in the opinion of either party, substantially modify the assessments which at present underlie the project.

/Any





Any variation of the loan agreement, so as to make it inconsistent with the industrial investment scheme that is approved by Parliament, would be subject to an amended scheme also being approved by Parliament.

I should be grateful if you would confirm that this letter represents your understanding of the agreement reached between us. .

*Yours sincerely*

*Edmund Dell*  
EDMUND DELL

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