

CENTRAL ELECTRICITY GENERATING BOARD

Sudbury House, 15 Newgate Street, London EC1A 7AU. Telephone 01-634 5111

From the Chairman  
The Lord Marshall of Goring Kt, CBE, FRS

14 June 1988

CONFIDENTIAL

The Rt. Hon. Nicholas Ridley MP,  
Secretary of State for the Environment,  
2 Marsham Street,  
London,  
SW1P 3EB

Dear Secretary of State,

SECRETARY OF STATE'S OFFICE	
TO <i>Mr Fremantle</i>	Copies to
FOR ADVICE (AND DRAFT REPLY IF APPROPRIATE)	<i>PS/SOS</i> <i>PS/RS</i> <i>PS/PUS</i> <i>Mr Guinness</i> <i>Mr Wilcock</i> <i>Mr Maclellan</i> <i>Mr Dart</i>
PLEASE BY:	
VIA <i>URGENT</i> <i>PS/MOS</i>	<i>Mr Moss</i>

LARGE PLANT COMBUSTION DIRECTIVE

I understand that the German Presidency is making a determined effort to secure agreement for this directive at the meeting scheduled for 16 June. If they succeed there will be adverse implications for electricity privatisation. In Cecil Parkinson's absence abroad, I thought I should write to you directly with my views.

You will know that in support of the Government policy, as set out in Cmnd 9397, the CEGB is actively pursuing a strategy leading to a downward trend in sulphur dioxide emissions from the 1990s. We have announced plans to retrofit 6000 MW of existing generating capacity equivalent to three 2000 MW stations. We estimate this voluntary programme will cost some £660 million. This scale of commitment properly reflects our developing understanding of the science but no more can be justified. Alongside should be seen our plans for ensuring that all significant new capacity will be essentially free from sulphur emissions e.g. nuclear or clean coal with full FGD, or renewables.

The effect of the proposed directive will be to superimpose a major compulsory retrofit programme above and beyond the voluntary programme. On our best estimates the German

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proposals in undiluted form would involve an additional commitment by the CEGB's successor companies equivalent to five major retrofits costing £1100 million. It would involve retrofitting plant with a residual lifespan after FGD commissioning of less than 10 years - an economically absurd proposition. Even a so-called "compromise" formula, to achieve a 60% rather than 70% reduction, would require three further retrofits costing some £700 million. On top of the cost of the initial programme, and perhaps also allowing some £300 million to secure NOx requirements, it could bring our successors' commitment to approaching £1700 million, on readily foreseeable costs alone.

Even more important than the total capital requirement for new expenditure is the incidence of that expenditure and its impact upon the ability of Big G and Little G to raise capital for the new investment that will be needed.

It is clear that, even on the most optimistic assumptions about the size of the future power station building programme and entry of new generating companies, both Big G and Little G will face a major investment programme to the end of the century. To a substantial extent this will cause each to rely on external borrowings, with a particular risk that investment in new generating plant - including nuclear, where funding demands are inevitably heaviest - will be curtailed by cash-flow problems and capital rationing enforced in practice by the exigencies of having to conform to City expectations when raising capital. At a time of such difficulties, to compel significant additional expenditure commitments on non-productive emission control investment of dubious real value would be a serious set-back - even if the costs are passed through to consumers. Without pass-through, the problems, for Big G at any rate, would seem insurmountable.

These matters will have to be spelt out in the prospectus. The result is bound to depress flotation proceeds. Moreover, it will be difficult to convince investors that such a retrofit programme is stable and will endure. They may well perceive a risk of further demands being added over time to a baseline target which for the UK starts off unjustifiably high in business terms. I therefore strongly urge you and your colleagues to proceed with caution in considering any proposals for additional requirements on top of the present voluntary programme. Even for that, full cost pass-through with a proper return on capital will be essential.

Nevertheless, if, despite these implications, you and your colleagues instruct that, for political reasons, it is necessary for the UK to support the proposed directive, we and our successors in Big G and Little G will of course comply to the extent (with cost pass-through) it is within our financial ability to do so.

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I am copying this letter to the Chancellor of the Exchequer, and the Secretary of State for Energy.

Yours sincerely,

*Walter Marshall*

Marshall of Goring