



10 DOWNING STREET

cc MASTER SET

From the Private Secretary

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12 September 1984

CAA REVIEW

The Prime Minister held a meeting yesterday to discuss issues arising from the CAA's review of air transport policy. Present were the Chancellor of the Exchequer, the Lord Privy Seal, the Secretaries of State for Trade and Industry, Transport, the Chief Whip and the Solicitor General. Also present were Sir Robert Armstrong, Mr. Gregson and Mr. Redwood. The meeting had before it the paper circulated by the Secretary of State for Transport as C(84)22.

The meeting discussed the implications of the various Laker law suits of which the most relevant were those brought by the Laker Liquidator and the class action brought by US lawyers on behalf of individual passengers. It was noted that Hill Samuel had advised that it would be possible for flotation to proceed if BA's directors were able to state, taking into account advice from US Counsel, that the US suits were unfounded and without merit. This was the course which BA hoped to follow. But it was noted that this advice was heavily qualified and it was far from clear whether BA would be in a position to make such a statement.

There were differing views on the extent to which the Laker cases presented an obstacle to privatisation. The damages sought were extremely large but against this it was argued that such claims for damages, with which US

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companies were familiar, were exaggerated. The litigation was likely to be long and drawn out and if the cases were indeed an obstacle they could remain so for a number of years.

It was suggested that Britain should go to arbitration in order to have the issue resolved under the Bermuda Agreement, though earlier advice had been pessimistic on the UK's chances of success. If the cases were lost there could be serious disruption to UK/US air services if British planes were impounded.

Summing up this part of the discussion, the Prime Minister said the Government should continue its efforts to resolve these disputes under the Bermuda Agreement. Consideration should be given to whether there was any way in which UK legislation could protect UK operators from action in the US Courts. It remained unclear how serious an obstacle the Laker suits presented. Meanwhile, the Government should decide what course it wanted to take following the CAA review.

The Prime Minister said the issues raised by the CAA review touched on important elements of the Government's philosophy - its wish to encourage competition and enterprise and to reduce the boundaries of the public sector. Some of these objectives were in conflict with one another. The Chief Whip reported that Government supporters were sharply divided between those opposing any transfer of routes from BA and those who believed it would be wrong to privatise BA without first creating a more competitive

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environment and a stronger base for the smaller independent air lines. The Prime Minister said the undertakings given by Sir John Nott could not easily be over-ridden.

The Secretary of State for Transport reported BA's proposal that B Cal should be allowed to compete directly with BA by increasing dual designation on a number of routes. While this was superficially attractive it did not, on examination, provide an alternative to route transfers. First, there was only a limited number of routes where dual designation was likely to be possible; secondly, heavy investment would be needed by B Cal to develop their share of the market (particularly given the handicap of using Gatwick) and they could cover the initial losses only if they had additional revenues from the transfers of some profitable routes.

Note was taken of the Foreign and Commonwealth Secretary's minute of 10 September which pointed out that transferring BA's Saudi routes to B Cal (and hence to Gatwick) would strain our relations with the Saudis and could mean a loss of business for the UK.

The Secretary of State for Trade and Industry and the Chancellor of the Exchequer suggested that B Cal could offer the Riyadh route which it had been allocated but which it was unable to use to BA in exchange for some other BA routes, e.g. the Caribbean which would mesh in well with B Cal's routes to Latin America and the Southern United States. This could enable Lord King to say that he had not

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been forced to surrender any routes and the Government to say that the Nott undertakings had been honoured. It was agreed that this proposal should be explored with Lord King.

If agreement could not be secured the only other way of meeting with CAA recommendations would be legislation to enforce route transfers. The Lord Privy Seal and the Chief Whip advised that this would be a perilous course which would divide the Government's supporters in both Houses. The Lord Privy Seal was also worried about the propriety of using legislation to transfer revenue earning rights to a private company.

The Prime Minister said the position of the smaller independents and the charter companies should not be overlooked. BA was in a position to use its financial muscle to cross-subsidise its Airtours subsidiary or to use surplus capacity on its scheduled routes to underline these airlines. It was argued that greater safeguards should be established against predatory practices either by strengthening the CAA or giving a greater role for the OFT and MMC.

Summing up the discussion, the Prime Minister said the Group were reluctant to pursue a legislative solution which would be extremely contentious and which would over-rule the Nott undertakings. The Secretary of State for Transport and the Secretary of State for Trade and Industry should contact Lord King in order to secure his agreement to an exchange of routes between BA and B Cal. They should also investigate how policing of predatory behaviour could be

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strengthened. Work should continue in an effort to clarify the implications of the Laker law suits. To allow time for this work to be completed the issue would not come to Cabinet on Thursday.

I am copying this letter to Len Appleyard (Foreign Office), David Peretz (H.M. Treasury), David Morris (Lord Privy Seal's Office), John Graham (Scottish Office), Callum McCarthy (Department of Trade and Industry), Murdo Maclean (Chief Whip's Office), Henry Steel (Law Officers' Department), and Richard Hatfield and Peter Gregson (Cabinet Office).

ANDREW TURNBULL

Miss Dinah Nichols,
Department of Transport.