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Prime Minister

PRIME MINISTER

existing managers } aware that MH intends to allow civil servants to bid for the contract to run

COMMERCIAL MANAGEMENT OF THE ROYAL DOCKYARDS - MANAGEMENT BID

Devonport Dockyard

3/12

As I mentioned to Cabinet on Thursday, there has been a welcome development in the process of transferring the Royal Dockyards to commercial management by 1st April 1987 of which you and colleagues should be aware as it raises issues of both principle and presentation.

2. A small team of senior managers at HM Dockyard Devonport, led by the Managing Director and including serving Royal Navy Officers as well as Civil Servants, have put together an outline plan to bid in competition with other companies for the contract to run Devonport Dockyard. They have held discussions in confidence with Plymouth City Council, with Peat Marwick Mitchell and with Barclays Merchant Bank; a limited company has been formed. The Managing Director has now written formally to us seeking confirmation that the Government would have no objection to a management bid and also asking what assistance, if any, we would be able to offer. I attach a copy of his letter. The team plan to make an announcement of their intention on 11th December but there must be a risk that their



initiative will leak locally before then. It may well be that the matter will be raised or even announced during the Second Reading of the Dockyards Bill on Monday

3. There are, of course, many precedents for management buy-outs. In this case, however, we are faced, for the first time, with a potential bid from Civil Servants for a large scale operation for which they have important day to day responsibilities. Before allowing the Managing Director to proceed I suggest we need to be satisfied on three main counts:

- a. that his proposals are consistent with our policy for the introduction of commercial management;
- b. that they have at least a prima facie chance of success;
- c. and that any conflicts of interest between public service and private interest can be resolved.

We have then to consider how best to present our decision.

Government Policy

4. Our aim is to introduce the maximum amount of competition into the task of refitting and repairing the Fleet. We need a strong pool of interested companies from which to select,



through competition, the future commercial manager. At Devonport the interest, though growing, is not as strong as at Rosyth and another viable contender is to be encouraged. The readiness of dockyard management to bid for the scheme should demonstrate support for our policy and have valuable presentational and industrial relations advantages.

Viability

5. The Managing Director and his team are at a very early stage in their plans and recognise that there are many commercial skills which at present they lack. But they have unrivalled experience of the main task and have already given careful thought to the outside talent they would need to recruit to make their proposal a strong runner.

Conflicts of Interest

6. I have looked to see whether we could, or should, adjust the top management of Devonport Dockyard to reduce the possibility of any conflicts of interest arising. Some minor changes in the responsibilities for dealing with prospective contractors may be needed but, at this stage, I believe there is a broad identity of interest between the Managing Director as a Ministry of Defence public servant and the Manager of the Dockyard as a potential bidder. For example in both roles he needs to demonstrate a commitment to supporting the Fleet, to



increased efficiency and to the future well-being of the workforce. I conclude therefore that for the moment, and provided we have undertakings, which we are obtaining, sensibly controlling the use of public facilities and private business during working hours, we should have no difficulty in accepting the position. There is also, inevitably, a degree of common interest, based on his own future employment prospects, between the Managing Director as public servant, as potential bidder and as a possible employee of the successful tenderer.

Balance of Advantage

7. The costs involved in preparing a bid could amount to some £250,000-£350,000 and I regard it as a strong sign of personal commitment that the Managing Director expects his senior management to put their own financial resources at risk from an early stage; they will however require additional backing, which they may not secure - and there is the risk that they may not win the competition. But the point at issue now is whether we should allow them to try. My strong recommendation, based on discussions my senior officials have had with the Managing Director, is that we should and, subject to the requirement that the competition for the contract must be seen to be fair, my Department will give them, and any other such in-house initiatives which occur, what help it can. Here I have in mind giving whatever assistance we would consider making available to



any competitor, as well as any which we could appropriately justify on grounds of advantage to the Department in the management of the Dockyard while it continues to be in our own hands. Throughout we would, of course, need to be careful not to attract justifiable criticism of giving unfair advantage.

8. The alternative - of not supporting them - will not necessarily discourage them since it is always open to Civil Servants to resign in order to pursue their interest; but their task will be substantially more difficult and our denial of help would undoubtedly be used against us. Nor would it be in our wider interest as we need the team to continue to manage the Dockyard through the difficult period immediately ahead.

Presentation

9. If we allow the Managing Director to proceed we run the risk of attack from two directions. On the one hand, our critics will say that we are giving undue advantage to our own employees - whose performance we have said we want to improve - and are not genuine in our search for a commercial solution: this could discourage the interest we seek from established private sector companies. On the other hand, we may be accused of abandoning our preferred scheme because of lack of commercial interest and opting instead for a form of management-led plc.



We shall need to handle the announcement carefully but I see no insuperable difficulty in refuting these arguments and using this new interest to the advantage of the Government and the Royal Navy.

Recommendation

10. In summary, I see advantage in publicly supporting the proposals of the Managing Director at Devonport that he be allowed to put forward a bid for the future management of the Dockyard. On the assumption that my colleagues will support this welcome development, I would hope to be free to make public reference to it at any time from the opening of the Dockyards Bill debate on Monday.

11. I am copying this minute to the Lord President of the Council, the Secretary of State for Trade and Industry, the Chancellor of the Exchequer, the Secretary of State for Scotland, the Lord Privy Seal, the Chancellor of the Duchy of Lancaster, the Secretaries of State for Employment and for the Environment, the Attorney General, the Minister of State, Privy Council Office and the Secretary of the Cabinet.

RMM

Ministry of Defence

29th November 1985

[Approved by the Defence Secretary
& signed in his absence]



IN CONFIDENCE

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0752 - 55 - Ext. 3987/3237

Our Ref: MD/PS 2048/149/2

The Right Honourable Michael Heseltine MP
Secretary of State for Defence

22nd November 1985

Dear Sir,

The purpose of this letter is to inform you that I and certain of my senior managers have been considering the options open to us with regard to the future management of Devonport Dockyard.

2 We are convinced that, with a relatively small injection of financial and commercial talent from industry, the existing management team and workforce at Devonport have the skills to transform the Dockyard into a highly successful business enterprise. This would benefit the Royal Navy, the taxpayer and the local community.

3 The introduction of commercial management by bringing in outside contractors, as currently proposed by the Government, is facing widespread opposition from employees, the local authority and many politicians. To secure the improvements that we know are possible at Devonport and to achieve a successful transition to the private sector, close and willing co-operation between the workforce and management with the support of the community is essential. This has led us to the conclusion that the operation of Devonport Dockyard by a management-led company, involving the employees, stands the best possible chance of success.

4 We propose to form a Company, structured along the lines of the National Freight Consortium, to tender for the contract to manage Devonport Dockyard. It is envisaged that whilst shares in the company would be held by management and employees, there would also be a shareholding by institutional investors and possibly the local authority.

5 In discussions with an international firm of Chartered Accountants and a London based Merchant Bank, it has been confirmed that our outline proposals appear viable and would be likely to receive the necessary professional and financial support. A great deal of further work is of course necessary before a fully defined set of proposals can be put forward. Before embarking on this more detailed work and broadening out the involvement amongst other senior managers, I would be grateful if you could confirm that the Government would have no objection to this method of achieving the commercial management of Devonport Dockyard. It would also be helpful to have an indication of whether the Government is prepared to make available every reasonable opportunity and assistance for the necessary professional work to establish the viability of the proposal.

6 Only a small number of people, including those who have advised us from the business sector, have been involved in the work so far. Whether the proposal is developed further or discontinued, it is our wish that the matter should not become public knowledge at present. May I therefore ask that this letter be treated in the strictest confidence.

Yours sincerely,
David Johnston

IN CONFIDENCE

SELECT COMMITTEE REPORT ON ROYAL DOCKYARDS

We welcome the Defence Select Committees continued interest in the future of the dockyards. We shall study their new report with care and there will be ample opportunity to discuss the points they have made during the Second Reading of the Dockyard Services Bill.

However, I note that the Committee agrees with the objective of infusing the Royal Dockyards with entrepreneurial dynamism and a spirit of competition is a laudable one and I still think that my Rt Hon Friend's proposals are the best means of achieving this

28 November 1985