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FILE

MJ

SUBJECT  
MASTER



Filed on:

10 DOWNING STREET  
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CC DTI  
FST  
CO  
Peter Owen  
Not Policy Unit

From the Private Secretary

21 November 1991

Dear John,

COAL PRIVATISATION

The presentation to the Prime Minister on coal privatisation on 13 November was attended by your Secretary of State, the Secretary of State for Trade and Industry and the Financial Secretary. Mr A. Rosling (Policy Unit) and Peter Owen (Cabinet Office) were also present.

I would be grateful if the recipients of this letter would ensure that it is seen only by those with a strict need to know of its contents and that no further copies are made.

The presentation developed the main points set out in your Secretary of State's minute of 3 October. It was noted in particular that British Coal (BC) had liabilities of £2.5bn-£3bn; and that the main recommended options for disposal were sale as a single company, sale of two balanced units, or sale as three companies, with Scotland separate. A further report on core options was scheduled for January.

After the presentation, your Secretary of State said that the main objective should be to secure the largest economically viable UK coal industry in the longer term. An important factor would be the ability of BC management to secure the additional 10 per cent reduction in unit costs which would be necessary to maintain the level of supplies to the generators at 40-50 mt rather than 30-35 mt by the mid-nineties. BC now had strong leaders who, he believed, could achieve the extra cost reductions. But their position would be undermined unless there was a constructive response from all parties, including the regulator and the Regional Electricity Companies (RECs) when BC entered into negotiations on medium-term contracts with the electricity generators early in 1992. The Government should play a part in facilitating this process. A successful outcome on these contract negotiations would also affect the value of BC when it was privatised. The number of companies to be offered for sale needed further consideration. A final decision was not required immediately, but it would be helpful if further work could be focussed on the preferred options.

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In discussion the following main points were made.

- a. Existing stocks of coal were already greater than the amounts judged necessary for a strategic reserve to maintain electricity generation during prolonged industrial action by miners. Even if these stocks were exhausted, it would now be possible to continue indefinitely by burning oil and opencast coal. Deep mining was no longer of strategic importance.
- b. The sharp reduction in the size of the coal industry that was foreseen reflected underlying economic realities and had nothing to do with privatisation. This point would need to be emphasised. The Opposition's policies were illogical: they proposed both to maintain the size of the coal industry and to increase the use of gas. Attention should be drawn to the environmental benefits of reduced reliance on coal.
- c. 19 pit closures were planned for the financial year 1992/93, but there would be few in the early part of the year when production was expected to be at high levels.
- d. It would be important to ensure that the reduction in coal prices arising from the rationalisation of the industry flowed through to electricity consumers and was not simply retained by the generators.
- e. The closures would have a major impact in certain areas including Nottinghamshire. To cushion the effects it would be necessary to ensure that RECHAR funds were released by the Commission, and consider the scope for inward investment projects and increased activity by BC Enterprise. Many of the redundant workers would have valuable skills. It was also necessary to look again at redundancy terms.
- f. If the Government stood back from the contract negotiations, the aim of achieving the largest viable industry would not be achieved. The generators would prefer a smaller industry, so that they were less reliant on a single fuel; and BC would also prefer a smaller and more competitive industry, with the Government picking up the costs of contraction.
- g. The Government's role in the negotiations would need to be carefully defined. The starting point should be a guaranteed lower price for coal. It would take time to realise the necessary cost reductions in the coal industry. But the critical negotiations with the generators on new contracts were only a matter of months away. The renegotiated contracts must be used to build confidence and help to ensure that cost reductions were achieved. The electricity industry was not a free market; and the regulator would be unlikely to intervene while the RECs had a monopoly if it could be shown that cooperation would produce the lowest prices for electricity consumers.

h. There should be a presumption against selling BC as a single unit. A range of 2 to 4 successor companies might be preferable.

The Prime Minister, summing up the discussion, said it was agreed that the aim should be to secure the largest economically viable coal industry; and that to achieve this aim it would be appropriate for the Government to play a carefully defined facilitating role in the negotiation of medium-term contracts for the supply of coal to the generators. It would be important to establish the views of the regulator at an early stage. Closures would be clustered in particular areas and could have a major social impact and lead to concentrations of dereliction. Further work should be undertaken on redundancy terms, and planning should begin now for replacement investment within existing structural programmes. In further developing plans for sale of BC the strategic aim should be to secure the maximum spread of ownership consistent with financial viability.

I am sending copies of this letter to the Private Secretaries of the Ministers who attended the meeting, to the officials who were present, and to Sir Robin Butler.

*Yours ever,*

*Barry*

Barry H Potter

John Neilson, Esq.,  
Department of Energy.

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MR POTTER

cc Mr Burr

COAL

1. In response to popular demand, I attach a draft minute on the coal privatisation discussion. It may not be as helpful as those who requested it imagined.
2. Since I was not expecting to produce a formal note, and my recollection of the meeting has faded a little, the minute is unlikely to be up to the usual standard (though the more obscure passages are not necessarily least faithful to the discussion) and I would be grateful if you would cross-check carefully against your own record.
3. I am also not too sure who was present.

*P F*

P F OWEN

21 November 1991

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(1) Can be done

- if BC reduce costs / capacity.

To keep 1. even coal industry.

(2) What restructuring? True-scale

Capacity > demand.

Uncompetitive

(3) Must start exp. contracts now.

Contract ~~has~~ signed mid-'92.

Cap. needed to be reduced '93 onwards.

(Bal. of Shute is sub-future).

Notes 57 - (35) - 92.

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Priv.

- Open Access Regions.
  - Offer Pits to Priv. Sector.
  - Return small asset packages.
- 

Foreign Ownership. ??

Hanson is the largest  
Coal owner!

I. Contracts or proposals.

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II. Cost reduction programme.

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III. More work on Str. options.

IV. Want 10 yr. offsh. coal. (VITAL).

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V. Policy impact. / Social impact. ✓

VI. Redun. Terms. ✓ → Clean Coal Technology.