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E(81)107

COPY NO 65

27 October 1981

## CABINET

## MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

## REGIONAL DEVELOPMENT GRANTS: POSSIBLE CHANGES

Memorandum by the Secretary of State for Scotland

1. I see very serious difficulty in the conclusions reached by the Secretary of State for Industry in E(81)101 both in regard to the possibility of denial of regional development grants to Sullom Voe and Flotta and to the possibility of a reduction in the rate of RDGs in order to provide possible option cuts.

Sullom Voe and Flotta

2. I accept the argument that payment of grant in these cases is not an effective use of public money; and I acknowledge that I have no direct Departmental interest in terms of public expenditure in this decision. But I consider it almost impossible for the Government to defend a decision to deny grant at this late stage when the terminals are built and in operation and when the Companies have been led to expect by us, both in general public statements and in particular dealings with them, that grants will be paid. I note the Attorney General's view that, in relation at any rate to the public pronouncements from Department of Industry, a refusal to pay grant on public expenditure grounds would be unlikely to be challenged successfully in the Courts. I gather that there is some doubt as to whether this view would hold good in relation to particular exchanges between the Department and individual Companies. But it is not so much the risk of legal challenge which concerns me as the potential damage to the confidence of Companies investing in the North Sea - on which, for instance, we have now decided to rely for the landing of associated gases as well as the oil resources. And my concern goes wider than that: I think that the confidence of industry generally in regional policy and indeed in the Government's commercial integrity would be badly shaken by the denial of RDGs to Sullom Voe and Flotta.

Rates of Grant

3. However while I have grave misgivings on grounds of good faith about a decision against payment of grant for the two oil terminals I am very much more concerned at the possibility of a general reduction in rates of RDG. This is a matter in which I have an acute and direct interest and I am most strongly opposed to any such possibility. In my view it would be completely mistaken to reduce industrial incentives at a time when industry is struggling through the worst recession since the war. Coming on top of recent increases in interest rates this would undermine still further industrial confidence in the assisted areas and be an additional set back to any hopes we had of modest recovery in the year ahead. From my own recent visit to the United States where I met some of the companies with whom we are in negotiation about possible developments in Scotland I know how finely balanced their decisions are and indeed I was pressed very hard on several occasions to give assurances about the stability of our regional measures particularly the availability of RDGs which are of course not on a contractual basis. If we make a change in the rate now I am convinced that we stand to lose development from some important companies who are at an advanced stage of negotiation and others will quickly see how easily they can be caught by changes in the rules and will therefore be much more hesitant to consider investment here. Such instability seriously reduces the cost effectiveness of the money we spend on regional industrial support.

Other Points

4. The Secretary of State for Industry comes to conclusions on two other possibilities in his Paper - the exclusion of capital intensive projects from eligibility for RDGs and - as an offset to the savings otherwise proposed - a reduction in the period of "imposed deferment" of payment of RDGs from 4 months to 2.

Eligibility of Capital Intensive Projects

5. I agree with the arguments advanced in favour of the continuing eligibility of capital intensive projects for RDG. This is desirable for potential North Sea oil developments: indeed continuing eligibility or, failing that, some saving provision is essential for Moss Morran in view of Ministerial commitments; and continuing eligibility could well be of critical importance to developments by BP at Grangemouth. However I would be prepared, in order to prevent the possibility of cuts in RDG even harsher than those indicated in the Secretary of State for Industry's Paper, to accept as a lesser evil the exclusion of capital intensive projects.

Period of Deferment

6. I would of course welcome a reduction in the period of deferment in the payment of RDGs, but it does not seem to me a sensible use of resources to offer this reduction as an offset to the savings being contemplated. The effect would be that in this first year the offset would substantially exceed the saving, and indeed the "saving" - which in my view would seriously threaten the stability of regional policy - would scarcely overtake the "offset" over the life of the present Parliament. I would very much prefer therefore that any such resources should be applied to avoid a cut in the rate of RDG.

G.Y.

SCOTTISH OFFICE

27 October 1981