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CABINET

MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

FIXED CROSS-CHANNEL LINK

Memorandum by the Secretary of State for Transport

PURPOSE

1. The purpose of this paper is to bring my colleagues up to date on the progress of the Anglo/French studies and to seek their guidance on whether we should be prepared to modify our presently stated criteria on private sector financing to accommodate a French requirement for reciprocal Governmental guarantees to cover the risk of unilateral abandonment for political or other reasons.

PROGRESS OF STUDIES

Technical

2. All forms of link proposed by the various British promoting groups (see Annex A) have now been subjected to a searching technical analysis. The Study Group has concluded that the only type of link on which an early start could be made is some form of bored rail tunnel with or without a vehicle shuttle. The technical unknowns, the marine and other risks associated with fixed structures and their erection are such that all other forms of link would require prolonged study before the two Governments could be satisfied that they were feasible and the residual risks acceptable. These and other considerations are developed further at Annex B.

Economic

3. The various drive through schemes are currently being subjected to a preliminary economic analysis to indicate whether or not they are likely to show returns significantly better than those for bored tunnels.

4. The preliminary economic analysis of bored tunnels on which I reported in E(81)124, which served as the basis for our last discussion in November has been further refined.

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5. However, the economic case for any fixed link depends crucially on the time and cost advantage that the various kinds of link could offer compared with the development of existing services. Dover Harbour Board, representing port and shipping interests are still working on their final report. Some advance material has been received and my officials are now co-operating with officials in the Department of Trade on an evaluation of the DHB case that ferries could cope with all foreseeable growth in traffic at unit costs considerably below present tariff levels.

6. I hope to return to the Committee in March with a fully developed analysis. The range of uncertainty is such that it is one to which a large element of judgement will have to be applied.

Organisational and financial

7. On the French side a Channel link would be a public sector enterprise. No basic incompatibility is seen between this and our own requirement that on this side of the Channel it should be a private sector undertaking. It is considered that appropriate forms of organisation can be developed both for the construction and operating phases. The possible involvement of the European Community in some way is a matter on which we would need to reach a view with the French at the appropriate time. The possibilities are under study by officials.

OPTIONS FOR DECISION

8. The issue before us in March will be whether:

- i. to have no fixed link
- ii. some form of bored tunnel is desirable, an early start on which would imply legislation in the 1982/83 Session;
- iii. to defer a decision pending further studies, which could take several years, of drive through schemes such as bridges and immersed tubes.

9. I will by then have received the full report of the Study Group, should have a clearer idea of French attitudes and will be in a position to submit a paper dealing comprehensively with the technical, economic, financial and other considerations which will enter into our decision.

10. If I am to do so, however, I need preliminary guidance on handling of the guarantee problem which will reflect on the ability of the British promoter to raise finance and on the acceptability of the total package he is able to get together.

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GUARANTEES

11. Our position has been that contingent liability on the public sector should be minimised. We have accepted that there could be a guarantee against political cancellation. We have told promoters that they should not assume that the Government would be willing to fund or guarantee cost over-runs on construction and have pressed them in the direction of securing commercial stand-by facilities.
12. The French have, from the outset of the discussions between officials, indicated that, if there were to be a link they would require, and would reciprocate, guarantees from the UK Government that all their costs would be reimbursed if work on the link was abandoned either as a result of a decision by the British Government or of failure of its chosen instrument. My French colleague repeated this requirement when I last met him. If we eventually decide to have a link we shall have to provide reciprocal guarantees.
13. The provision of reciprocal guarantees can also be used as a bargaining counter to persuade the French to drop their instinctive wish that Governments should be able to regulate tariffs. Officials advise that, if we can meet the French on reciprocal compensation guarantees, it should be possible to get them to accept arrangements which would ensure the essential commercial freedom (with safeguards only against abuse of monopoly) which promoters will need.
14. If there are to be reciprocal compensation guarantees, both Governments would be bearing ultimate responsibility for the performance of their chosen instruments. In this situation, finance raised for the project in the capital markets would not be competing on equal terms with private sector projects. We must accept, therefore, that genuine private risk capital is no longer an option, and we shall have to rely on the 'hybrid' financing arrangements of the kind identified by the NEDC Report on the financing of nationalised industry investment.
15. Given the contingent liability of the Government to Government guarantee, the prudent approach would be to reinforce the position of the UK promoter by issuing a completion guarantee. This would be a minimum departure from our original intentions and would not affect the efficiency we would expect from the private sector in constructing and operating the UK element of the link.
16. The sort of structure I have in mind is one under which the promoter would secure a commitment from market sources to provide finance for the initially estimated cost of the link and for a specified and substantial amount of cost over-run. In the event that the promoter needed further finance which could not be raised on the market and the Government guarantee were called, the promoter would lose all or part of his equity share in the link and could face additional financial penalties. There would be every incentive to find market finance on more favourable terms, thus reducing the risk that the guarantee would be called. But if in the last resort the Government had to take over the equity it would be open to it to try to find another promoter and sell its interests.

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17. The aim of the arrangements would be to leave with the UK private sector the decision as to whether the prospective return justified the risk, would ensure that the risk remaining with the private sector interests was so substantial as to correctly motivate them and that the risk of Government involvement was kept to a minimum.

18. We have been told by the promoting groups and their financial advisers that such a completion guarantee would make it much easier for them to raise finance on a basis less dependent on the contracts from British Rail and the Continental railways for the allocation of paths through the tunnel: we have emphasised that we would not allow BR to contract on a basis which placed on it a disproportionate share of any risks arising from shortfall of traffic.

Conclusion

19. I should be glad to know whether, reserving entirely the decision on whether or not a link should be built, my colleagues agree that the French requirement for reciprocal guarantees (as specified in paragraph 12) should be accepted; that I can carry forward discussions with the French on this basis; and that I should further explore possible hybrid financing arrangements.

D A R H

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SCHEMES SUBMITTED

[All costs are for link plus coastal terminals (including BR) and are at January 1981 prices]

Bored TunnelsBritish Rail/SNCF

- Single 6m tunnel for conventional rail traffic. Cost £879m.

European Channel Tunnel Group

(Costain
Royal Bos Kalis Westminster
Phillipp Holzmann
Spie Batignolles)

- Originally proposed their own 6m scheme but now working on joint promotion of BR's scheme.

Channel Tunnel Developments 1981

(Tarmac
Wimpey
Robert Fleming & Co
Kleinwort Benson)

- Single 7m tunnel for conventional rail traffic plus a vehicle ferry. Cost £1374m. Or, twin 7m tunnels either phased (cost £1785m) or unphased (cost £1682m).

Anglo-Channel Tunnel Group

(Taylor Woodrow, Balfour
Beatty and Edmund Nuttall)

- Either 6m or 7m tunnel. Cost about £1100m.

Immersed TubeLaing

- IT providing dual two lane road link with or without double track rail link. Cost £3390m with or £2345m without.

BridgesLinkintoeurope

(Headed by Sir Ralph Freeman)

- Multi-span suspension bridge for dual three lane motorway. Cost £1950m. Single 6m rail tunnel as optional extra. Total cost £2830m.

EuroBridge

(International Group of
Consultants)

- Multi-span suspension bridge for dual four lane motorway. Cost £3500m. Single 6m rail tunnel as optional extra. Total cost £4400m.

Viaducts and TubeEuroRoute

(British Steel - Redpath Dorman
Long
British Shipbuilders
Fairclough Construction
John Howard & Co Ltd
Sir Robert McAlpine & Sons Ltd
Trafalgar House
Raymond International Builders Inc)

- Inshore viaducts with central immersed tube for road link. Rail link in immersed tube throughout. Cost £4000m.

CHANNEL LINK
ANGLO-FRENCH STUDIES

REPORT ON PROGRESS

Technical Studies

1. All the options for a fixed link - bored tunnels, bridges, submerged tubes and a combined bridge/immersed tube - are being examined with reference both to the general problems associated with each type and to the particular difficulties attendant on construction in an international waterway. Broad agreement has been reached that the options fall into two main categories:

bored tunnels where the technology is relatively well proven and no problems of maritime safety are involved; and

the remaining solutions where, to a greater or lesser degree, innovatory design concepts, materials or construction techniques are involved and major issues of maritime safety, law and ecology arise.

2. Significantly different timescales are, therefore, inherent in the two categories of scheme. Construction of a bored tunnel - aided by the experience of the previous project - could begin after a relatively short period for preparation and design. By contrast, the international maritime authorities would further extensive studies and consultations with/be necessary to establish the feasibility of the other schemes before a decision in principle could be made in favour of one of them. The study group is concentrating on identifying more precisely the work that would be involved in this feasibility testing in order to evaluate the difference between the timescales for the two categories of scheme.

Economic Studies

3. The key question is whether the development of the existing modes of crossing the Channel could cater more effectively for the predicted levels of traffic than any of the forms of fixed link. The answer to

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this question depends partly on how the total market would grow (both in the absence of a fixed link and as a result of generation by the link) and partly on what improvements in relative competition the existing modes would be able to achieve. The various assumptions about traffic, tariffs and operating costs adopted by the different promoters are being examined critically, using a range of figures and sensitivity testing. The material being provided by the Dover Harbour Board and the principal ferry operators in support of their case for relying on the development of the existing sea services is also being examined.

4. The calculations of the transport costs and benefits of the tunnel options compared with the present modes (referred to in the previous memorandum) are being refined and extended to include the drive through road links. Preliminary results indicate that all of fixed link offer broadly similar positive returns on central assumptions, but that the optimistic-pessimistic range is wider in the case of the road links, reflecting their greater uncertainties of construction cost and traffic generation.

5. It has been agreed that the impact of a fixed link on employment, regional development, the landward environment, etc in each country should not form part of the joint studies, but that each side should examine these factors separately from its own national viewpoint in whatever manner it felt most appropriate. Work on this is in hand. Likewise the returns which the respective national railways would secure from any investment which they made in association with a fixed link are being considered separately. The assessment for British Railways takes into account the wider effects resulting from secondary traffic generated by the link and from the displacement of existing services. Work on this is still in progress between the British Railways Board and the Department. Preliminary results indicate that the Board would

secure a positive return - even in adverse circumstances - if the financial arrangements made with and by the tunnel promoter were as recommended by the Board's principal banking advisers.

Financial/Juridical Studies

6. The studies have concentrated on how best - having regard to the experience of the previous project and the different basis of financing on the two sides of the Channel - a fixed link could be developed and operated in terms of corporate structure, the division of risks, costs and revenues, and the rights and liabilities of the parties. The balance of advantage is likely to rest in favour of having distinct UK and French entities, each of which would be responsible (within the context of an agreed specification) for the execution and cost of part of the construction, with subsequent revenues divisible in a manner that reflected initial estimates and not out-turn expenditure - thereby maximising incentives to efficiency and minimising the need for cumbersome liaison machinery. Consideration is being given to what the rights and liabilities of each entity should be in the event of poor performance or default by the other.

7. Consideration has been given to the supervisory role of the Governments and the question of inter Governmental guarantees. These issues are discussed in the main body of this memorandum.

8. The possible involvement of the European Community has been noted as a matter requiring later consideration. The implications for the UK of such involvement are under study by officials.