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cc BG.



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The Rt Hon Lord Young of Graffham
Secretary of State for Trade and Industry
1 Victoria Street
LONDON
SW1H 0ET

11 January 1988

Prime Minister

Contact with Mr. Channon's
approach?

Dear David

PRC6
12/1

No, I am
worried about this
line - see bottom
of P2. not

BRITISH AIRWAYS AND BRITISH CALEDONIAN: ENQUIRIES BY EUROPEAN COMMISSION DGIV

British Airways gained control of British Caledonian on 21 December. They are now in the process of consolidating the merger. They aim within the next couple of months to transfer all BCal's business to British Airways Plc and to integrate the scheduled services of both airlines within the single company.

Also on 21 December Commissioner Sutherland, despite your and my attempts to dissuade him, wrote to both British Airways and BCal informing them that the analysis carried out so far by the European Commission suggested that, if the merger were to proceed in the form proposed, it could constitute an abuse of a dominant position within the meaning of Article 86 of the Treaty. Commissioner Sutherland said that he had instructed his officials to explore with each company, should they so wish, the issues raised. The letter reached BA too late to affect its bid for the BCal shares.

BA have reacted to the Commission's approach in a firm but conciliatory way. Though expressing surprise at the Commission's intervention, and its timing, they offered discussions, which took place in Brussels on 5 January. The outcome of these was that BA, while in no way conceding that the Commission were justified in intervening, agreed to provide them with a lot more information, with the aim of refuting the charge that they were abusing a dominant position. They intend to present this information at a further meeting with the Commission this Friday 15 January.

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BA are prepared for subsequent events to take two possible courses. It may be that DGIV (who seem to want to move the matter forward quickly) will signal their willingness to reach an early settlement whereby, in return for modest concessions from BA, they would withdraw the threat of further action. BA would be prepared to contemplate such a settlement if the terms cost them little (they are most unlikely to go along, for example, with the surrender of further routes). Alternatively, if the Commission press their charge that BA is abusing a dominant position and demand remedies that BA regard as unacceptable, then BA will play for time, taking every opportunity to challenge the Commission's competence and its case, if necessary in the European court.

BA's handling of the approach from Commissioner Sutherland is their own business; but they seem to me so far to have acted sensibly. I certainly would not propose to dissuade them from reaching an early settlement with DGIV should they find acceptable terms on offer.

There is one other aspect of this affair we have to consider. A little before Commissioner Sutherland's approach to BA and BCal, on 10 December, DGIV wrote to UKRep requesting HMG's "assistance pursuant to Article 89 of the EEC Treaty, in the investigation of the compatibility of the proposed merger....." DGIV went on to ask for various information about BA's and BCal's evidence to the MMC, about statistics of airline operations, about air services agreements between the UK and other countries, and about our own air transport licensing requirements. UKRep sent an interim reply while officials considered the Commission's competence to request this information.

Departments' legal advisers have now discussed the matter. I understand they consider that we should not be on strong ground in refusing the Commission's request completely. My own view is that we should not give the Commission any help in this matter outside our legal obligations or our clear self-interest: DGIV's intervention is unnecessary, untimely and officious. But I am prepared to accept that, regardless of our legal obligations, a total refusal to respond would be counterproductive in our relations with the Commission, and not helpful to BA's guardedly conciliatory approach. I therefore agree with the official advice we have received that we should answer the Commission's questions selectively - wherever we have the information available and we see no objection to its provision. My officials are preparing a draft response on this basis and plan to send it to UKRep for delivery to the Commission later this week, once it has been agreed with your own Department, FCO and government lawyers.

This letter is primarily to bring you and other colleagues up to date with developments on this issue over recent weeks. If, however, you or others have any comments on the line I am taking I should be grateful to have these by Thursday morning.

Continued....

No -
Surely
it was
given
in
confidence
strictly
for the
purpose
of the
forum
in the U.K.

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I am sending copies of this letter to the Prime Minister, the Chancellor of the Exchequer, the Foreign Secretary, the Attorney General, and Sir Robin Butler.

V
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Paul

PAUL CHANNON

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