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Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000 / February 1982

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Prime Minister

The Rt Hon Nigel Lawson MP
Secretary of State for Energy
Department of Energy
Thames House South
Millbank
LONDON SW1P 4QJ

E(N1) agreed on 2 November
that draft Nationalised Industry Objectives
should be circulated before Christmas. As
you will see, progress has been slow.
Robin Ibbes suggests I write round

Dear Nigel

NATIONALISED INDUSTRY OBJECTIVES

Robin Ibbes has sent me a copy of his letter of 22 January
to you about draft objectives for the NCB, ESI and BGC
prepared by your Department.

asking for the remaining objectives to be
circulated before end February. Agree
I do so?
Mus 2/2

I must say that I generally share his reaction to the present
drafts. The aim of having objectives was to provide an agreed
and lasting basis for Government/industry relations; as a
framework to guide successive Corporate Plans; and as a
measure for judging the success of management. To serve these
purposes the statement of objectives needs to tackle and
resolve long-term issues about the purpose and shape of the
industries, some of which will be contentious. If we are to
use the objectives as the basis of a better relationship with
the industries they will have to address these difficult issues
despite the temptation to defer them until later.

*Yes
ms*

I appreciate that there are special circumstances in the NCB
and CEGB when new Chairmen are to be appointed during the
year; and for BGC where important legislative changes are
under way. This may affect how far we can go in getting agreement
with the industries in the short term. But it should not prevent
us from clarifying our own thoughts. We shall in any case need
to be in a position to brief an incoming Chairman clearly on
many of these matters.

I do not want to comment in detail on the questions suggested
by Robin Ibbes about particular industries. Generally they seem
to me to raise important and relevant issues. Indeed one
additional question which could usefully be added is about the
role of private capital in both the NCB and ESI. This is a
question for the longer term but in this context one that is
worth thinking about now.

/I am copying

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I am copying this letter to the other members of E(NI) and to Sir Robert Armstrong.

[Handwritten signature]

GEOFFREY HOWE

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bc A Inquard

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10 DOWNING STREET

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D/IND
D/TRADE
D/TRANSPORT
CS, HMT
D/N
D/M

Nationalised
Industries

3 February 1982

From the Private Secretary

Nationalised Industry Objectives

The Prime Minister has been following the correspondence between the Department of Energy, CPRS and the Treasury about draft nationalised industry objectives for the NCB, ESI and BGC.

The Prime Minister has asked me to remind Departments of E(NI)'s remit on 2 November to sponsor Ministers to submit draft objectives for nationalised industries to the Committee. The Prime Minister would be grateful if this was done before the end of February.

I am sending copies of this letter to the Private Secretaries to the other members of E(NI) and to David Wright (Cabinet Office).

Mes

John Kerr, Esq.,
H.M. Treasury.

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Rt Hon Nigel Lawson MP
Secretary of State
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LONDON SW1

29 January 1982

D. Nigel.

NATIONALISED INDUSTRY OBJECTIVES

I have seen a copy of your Private Secretary's letter of 23^{below} December enclosing draft objectives for those nationalised industries which your Department sponsors. Before we meet in E(NI) to review the question of objectives for all nationalised industries it may be useful if I set down three points I think that all the drafts should reflect.

First, I believe that all objectives should deal with the question of industrial relations (IR). I understand that IR are specifically mentioned in the enabling statutes of most nationalised industries, and we have agreed that the industries should encourage the development of employee involvement. I suggest that something on the following lines should be included in all objectives:

"To maintain proper machinery for the conduct of good industrial relations; and to develop and improve arrangements for involving employees and their representatives in policies and decisions which effect their working lives through the provision of relevant information and arrangements for consultation."



Secondly, I doubt whether a requirement to provide "adequate" training (BGC's ninth objective and NCB's fifth) can be reconciled with the objectives of the New Training Initiative which contemplate, for example, wholesale reform of our present skilled training arrangements. In fact, I am not at all sure that any general objective on this subject can be expected to offer management much useful guidance. And if an objective is too tightly drawn, they might argue that it precluded them from taking part in a training scheme which produced wider community benefits. However, if my colleagues would like to see an objective on this subject, I should prefer it to be rather firmer in time, perhaps in these terms:

"To see that all employees receive training which is necessary to enable them to contribute fully to the efficient operation of the undertaking".

Thirdly, I was very glad to see the unequivocal reference to privatisation in BGC's seventh objective. I am sure that something on these lines should figure in the objectives for any industry where there is any prospect of progress on this front in the foreseeable future.

On a more general point, I am concerned that we should not lose sight of what should be one of the main aims of this exercise, that of controlling unit labour costs in the nationalised industries. The broad objectives in the present drafts provide adequately for this in their reference to costs, but what matters more is how that is developed in the detailed performance aims which are to be set for each industry. We need to ensure that these cover, among other things, measurable and regularly-monitored performance indicators on unit labour costs. While some progress has been made on the preparation of performance aims, much remains to be done and I hope we can agree that work should proceed as quickly as possible.

I am copying this letter to all members of E(NI) and to Sir Robert Armstrong and Mr Ibbs.

29 JAN 1982





Nat. Incl.

CABINET OFFICE
Central Policy Review Staff

70 Whitehall, London SW1A 2AS Telephone 01-233 7765

From: J. R. Ibbs

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Qa 05785

22 January 1982

Dear Secretary of State,

Nationalised Industry Objectives

Your Private Secretary's letter of 23 December 1981 asked for my comments on draft objectives for the British Gas Corporation, the Electricity Industry and the National Coal Board.

I have to say that these provisional drafts by your officials do not seem to me to be yet in a form which would achieve the firm base for Government/industry relations aimed at in our Report. They are, as the covering letter says, very general, and do not go far beyond the statutory duties which are constantly referred to. Although we envisaged that objectives should be set in qualitative terms, with detailed figures to be filled in later in the reviews of corporate plans, the essential point is that the objectives should be clear statements of what Ministers require from each industry.

This will entail some fundamental thinking about the direction in which Ministers wish each industry to develop. I make some suggestions about each of the three industries later in this letter. I recognise that this fundamental thinking will not be easy, and will present some difficult choices for Ministers. But I am convinced that unless Ministers address these issues, and have worked out a very clear idea of their preferred longer-term development for each industry for discussion with the Chairman, more precise direction of the industries will not be achieved and the setting of objectives will have little value.

Fundamental thinking about Ministers' real objectives is the first stage. The second stage is to decide how best to put these across to the industry. There may be a preliminary question whether the objectives

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match the present statutes or whether the statutes need to be changed. It may be that the sponsoring Minister will decide, for tactical reasons, not to reveal all his objectives explicitly to the Chairmen in written form if this would lead to a pointless confrontation. For example, in some cases the objectives formally put forward might be limited to intermediate aims related to the length of the present Chairman's appointment - though certainly this should not be a general rule. In the extreme case, if the current Chairman will not accept a Minister's real objectives there will be a question whether these should be modified or the Chairman replaced. What is essential is that any difficulty envisaged in selling the objectives to the Chairman should not be allowed to be an excuse for not having them clearly defined in the Department.

Finally, as a third stage there will be a question whether objectives are to be published and in what form. I recognise that there may have to be some iteration, and what is to be published may reflect back on what is put to the Chairman. But I do not think it should be assumed from the outset that the objectives will be published without modification, or the result is likely to be bland and unhelpful.

There is one further point I should like to make on objectives for the energy industries generally. A main aim of policy in the past seems to have been to ensure that capacity is sufficient to ensure meeting national 'needs'. We are witnessing the costs of this in the shape of excess capacity in coal and electricity. For the future, world economic growth rates now seem to be on a lower trend than in the post-war period. Equally important, experience in the 1970s suggests a more unstable future. In this environment all businesses must become more flexible - and this needs to be reflected in the objectives of the nationalised industries. For each industry a fresh look will be needed on size of producing units, diversity of supply and more adaptability from consumers.

I now list some strategic questions which struck me on reading the draft objectives for each of the individual industries:

National Coal Board

- (i) Should it not be made explicit that the eventual goal is for the NCB to earn a positive rate of return on assets resulting in a

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reasonable contribution to financial self-sufficiency?

'Breaking even on historic cost basis without deficit and operating grants' is surely an intermediate objective.

(ii) Two important steps towards realising the intermediate objective of breaking even are to reduce the current over-capacity as rapidly as possible through accelerated pit closures, and to secure a greater willingness throughout the industry to face economic realities. Can some way be found of writing into the objectives that the Government regards these as essential aims?

(iii) Is not the aim to reduce overall unit costs in real terms a modest one? Will not the phasing out of high cost pits and the impact of the substantial investment in recent years make this almost automatic? Would not a more appropriate medium-term target be to reduce the average unit cost of those pits which are to continue?

(iv) Should the long-term aim be for the NCB to produce less coal than aggregate UK demand? This would ensure that imports retained a long-term foothold in the market to promote continuing competitive pressure. Is not the insurance policy of net exports too expensive in national terms? If this is accepted, then it should be made explicit to the NCB that there is no strategic need for UK demand to be met wholly from indigenous production. This would clearly have a direct bearing on the size of the investment programme since it would point towards lower demand scenarios with the flexibility to increase output in the medium term if these prove too pessimistic. What in any case is the NCB's flexibility to increase production?

Electricity

(i) A decision needs to be made on the structure of the industry and this in turn depends on what Ministers want from the industry. Do Ministers want a strong centrally controlled supply-led industry which would facilitate the introduction of nuclear power? Or do they want a more fragmented industry with supply and sales integrated

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on a regional basis which would result in greater customer responsiveness and a dilution of union power?

(ii) In the interests of preventing a recurrence of the present over-capacity does the standard of service need revising. Do Ministers consider that consumers would now be prepared to accept a higher possibility of brown-outs at winter peak demands in return for lower tariffs? A reduction in the plant planning margin, which is currently under examination, would be helpful.

(iii) If more capacity is installed, should one of the industry's specific objectives be to enhance supply flexibility by constructing between now and the end of the century only nuclear or coastal based power stations (thereby ensuring a continuing supply of coal imports)?

(iv) Should electricity pricing be made more responsive to commercial pressures by withdrawing the statutory requirement that there should be no discrimination between consumers?

(v) How should the industry interpret its objective in regard to its suppliers? Does it mean, for instance, it should try to retain two UK turbine manufacturers?

British Gas Corporation

(i) What will be the ultimate structure of BGC? Is it envisaged that it will be solely a trunk pipeline distributor of gas for third parties? Will its producing gas fields be privatised in the wake of its oil assets and retailing outlets? Will it be prevented from further exploration? Will the sales side be privatised on a regional basis? Will the seasonal storage facilities, in particular Morecambe, Rough and Canvey also be privatised? If so, what impact will this have on energy policy and security?

(ii) Once the long-term structure is decided, what profit centres for the industry are the most appropriate as the intermediary steps?

(iii) Is it intended that BGC will eventually become a manufacturer of synthetic gas to replace natural gas or will this be left to the private sector to develop?

(iv) What is the medium-term policy on domestic gas prices to be?

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I recognise that these fundamental questions (which are not intended necessarily to be comprehensive) will not be easy to resolve. At the same time, however, the value of defining objectives lies in reaching answers to questions such as these. Until Ministers decide on the long-term direction, the relationship with the industries is going to continue to be characterised by squabbles and drift. I need hardly say that in working out the objectives for each industry in more detail, members of the Review Staff would be very ready to join in discussions with your officials.

I am sending copies of this letter to the other members of E(NI) Committee, and to Sir Robert Armstrong.

yours sincerely,
R.L. Hill

01 211 6402

J R Ibbs Esq
Central Policy Review Staff
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23 December 1981

Dear Mr Ibbs,

NATIONALISED INDUSTRY OBJECTIVES

E(NI) Committee on 2 November invited sponsor Ministers to submit draft objectives to the Committee before Christmas. I attach draft objectives prepared by officials in this Department as a possible basis for discussion with the industries. As envisaged in the note which was sent to the NICG, they are drafted in a very general form, with a view to the possibility of developing them in discussion with the industries and to further elaboration and quantification in the industries' corporate plans. My Secretary of State has not yet been able to consider them but would welcome your comments.

The Government will be appointing new Chairmen to both the NCB and the CEEB around the middle of 1982. In the case of BGC, legislation has just been introduced which will enable the Government to make a radical alteration to the shape of the industry and which the Corporation will continue to oppose until it is enacted. In these circumstances, my Secretary of State feels that a discussion of objectives with these three industries in the near future would not be productive and that it would be better to defer such discussions until after the new Chairmen have been appointed and the Oil and Gas (Enterprise) Act is on the statute book. He also feels, though, that this need not prevent Ministers from continuing to clear their minds on objectives for these industries.

I am copying this letter to the private secretaries of members of E(NI) and to David Wright in the Cabinet Office.

Yours sincerely

David Lumley

DAVID LUMLEY
Private Secretary



C O N F I D E N T I A L

DRAFT OBJECTIVES FOR BGC

In a manner consistent with statutory duties and obligations:

1. to provide for an economic and efficient gas supply for Great Britain, in particular by:-
 - a. ensuring a reliable supply at an economic price to customers whom the Corporation have a statutory contractual obligation to supply;
 - b. extending gas supplies to other customers whenever it is economic to do so, and consistent with the requirements of fair competition; and
 - c. pursuing a gas purchasing policy which gives due weight to considerations of ^{fair competition, of} cost and ^{of} supply security in both the short and longer term, and which takes account of such guidelines as may be agreed from time to time between the Corporation and the Secretary of State.
2. To operate an efficient and economic gas transmission and distribution network for the carriage both of BGC gas and of gas being supplied by others via BGC-owned pipelines.
3. To operate within the financial regime agreed with Secretary of State and the Treasury including the financial target and external financing limit.
4. To improve operating efficiency and restrain costs in all areas, and to meet any performance aims agreed with the Secretary of State to this end.
5. To plan and implement a programme of investment, consistent with the objectives on the financial regime and on efficiency and costs above and in line with guidance from the Secretary of State on the overall size and shape of the programme, such a programme to be justified by reference to techniques of appraisal agreed with the Department of Energy, including the RRR. The Department of Energy will be consulted on projects of major size or particular importance.



C O N F I D E N T I A L

6. To set tariffs in accordance with general guidelines agreed with the Secretary of State and to negotiate contract prices in line with prevailing market conditions.
7. To identify and hive off into subsidiary companies peripheral activities not directly related to the main business for them to become candidates for privatisation, or in some cases, for joint ventures with the private sector and to take effective action to dispose of assets which have been identified as suitable for divestment.
8. To organise the remaining activities into separate profit centres so that the profitability of each can be clearly identified and monitored.
9. To maintain an adequate level of recruitment and training consistent with the Corporation's statutory obligations, these objectives, and the need to improve productivity.
10. To operate procurement policies consistent with these objectives along guidelines agreed with the Secretary of State with due regard to the long-term interests of UK suppliers, and in particular their international competitiveness.
11. To foster the Corporation's international consultancy service as a profitable business in its own right and in accordance with guidelines agreed with the Secretary of State.
12. To undertake research and development activities in accordance with a programme agreed with the Secretary of State.



C O N F I D E N T I A L

DRAFT OBJECTIVES FOR ELECTRICITY INDUSTRY

A. INDUSTRY WIDE

In a manner consistent with statutory duties and obligations:

- i. Meet the reasonable demands of consumers for a reliable and economical supply.
- ii. Operate within the financial regime agreed with the Secretary of State and the Treasury, including the financial target and external financing limit.
- iii. Improve operating efficiency and seek to reduce costs in all areas, and meet any performance aims agreed with the Secretary of State to this end.
- iv. Plan and implement a programme of investment, consistent with the financial regime agreed with the Secretary of State and the Treasury, and the objectives of improved operating efficiency and cost reduction. The programme should be justified by reference to techniques of appraisal agreed with the Department of Energy and the Treasury including the RRR. The approval of the Secretary of State will continue to be required for projects of major importance, involving significant capital expenditure. The Secretary of State may give guidance about the overall size and shape of the investment programme.
- v. Seek fuel economy and the efficient use of energy by means including the use of combined heat and power where economic, whether promoted by the industry or by others.
- vi. To set tariffs in accordance with these objectives, in particular (ii) and (iii) above concerning financial disciplines and performance aims agreed with the Secretary of State.
- vii. To operate procurement policies consistent with these objectives along guidelines agreed with the Secretary of State with due regard to the long-term interests of UK suppliers, and in particular their international competitiveness.
- ix. Develop closer working arrangements within the industry.



C O N F I D E N T I A L

B. ELECTRICITY COUNCIL

- i. carry out its statutory duties to:
 - a. advise the Secretary of State on questions affecting the electricity supply industry and matters relating thereto;
 - b. promote and assist the maintenance and development in England and Wales of an efficient, co-ordinated and economical system of electricity supply and to this end to foster closer working arrangements within the industry.

In particular:

- ii. Ensure it is in a position at all times to offer an accurate and comprehensive account of the industry's financial position to the Secretary of State.
- iii. Carry out a research and development programme according to plans agreed with Secretary of State; emphasis on work on nuclear power, renewable sources of energy, efficient use of energy and technological innovation - eg in the area of load control.
- iv. Provide, through British Electricity International Ltd, support to British exports.

C. CEGB

- i. Carry out its statutory duty to develop and maintain an efficient, co-ordinated and economical supply of electricity in bulk for all parts of England and Wales, consistent with industry objectives (i)-(x) of A above.

D. AREA BOARD

- i. Carry out their statutory duty to acquire bulk supplies of electricity and to plan and carry out an efficient and economical distribution of those supplies to persons in their area, consistent with industry objectives (i)-(x) above.



C O N F I D E N T I A L

DRAFT OBJECTIVES FOR THE NATIONAL COAL BOARD

In a manner consistent with statutory duties and obligations:

1. to operate within the financial regime agreed with the Secretary of State and the Treasury, including the external financing limit, and in particular to achieve an early return to breakeven on an historic cost basis without deficit and operating grants;
2. to improve operating efficiency and restrain costs in all areas so as to reduce overall unit costs in real terms, to meet any performance aims agreed with the Secretary of State to this end, and to permit prices to their customers which are fully competitive with the price of imported coal;
3. to plan and implement a programme of investment, consistent with the objectives on the financial regime and on efficiency and costs above and in line with guidance from the Secretary of State on the overall size and shape of the programme; such a programme to be justified by reference to techniques of appraisal agreed with the Department of Energy, including the RRR. The Department of Energy will be consulted on prospects of major size or particular importance;
4. to arrange for a secure and continuous supply of coal to that share of the energy market which the Board can hold on a lasting basis consistently with what is said above about profitability and prices;
5. to maintain an adequate level of recruitment and training consistent with the Corporation's statutory obligations, these objectives, and the need to improve productivity;

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6. to operate procurement policies consistent with these objectives along guidelines agreed with the Secretary of State with due regard to the long-term interests of UK suppliers, and in particular their international competitiveness;
7. to keep under review the organisation and scope both of their mining activities and of their non-mining activities and to discuss any major changes with the Secretary of State;
8. to carry out a research and development programme according to plans agreed with the Secretary of State.

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