

Ref. A085/241

PRIME MINISTER
_____Type 22 Frigates

C(85) 3

BACKGROUND

B — Cabinet decided on 19 July 1984 (CC(84) 27th Conclusions, Minute 5) that there should be a third round of tendering for the two Type 22 frigates required by the Ministry of Defence. This decision took into account the fact that the earlier tender submitted by Cammell Laird overestimated the extent to which that yard's overhead costs would be recovered from other work, and the problems created by the industrial disruption then occurring at Cammell Laird. The lowest third round tender was submitted by Swan Hunter, but the Secretary of State for Defence nevertheless proposed in this 18 December 1984 minute that one of the two orders should be placed with Cammell Laird. The Secretary of State for the Environment endorsed this judgment in his minute of 18 January 1985. The Secretary of State for Trade and Industry pointed out the difficulties arising from not accepting the lowest tender in his minute of 21 December 1984. The note by officials of the Department of Trade and Industry, Treasury and the No 10 Policy Unit attached to the Secretary of State for Trade and Industry's paper (C(85) 3) sets out the facts the Cabinet will need to bear in mind in deciding which yards are to receive the frigate orders.

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MAIN ISSUES

2. The main issues before the Cabinet are as follows -
- a. Should Swan Hunter receive both orders, or should one order be placed with Cammell Laird despite the need for a Ministerial direction to the Ministry of Defence Accounting Officer to this effect?
 - b. If one of the orders is placed with Cammell Laird, how should the additional costs to British Shipbuilders (BS), over and above the additional direct costs to the Ministry of Defence, be met?
 - c. If both the orders are placed with Swan Hunter, what steps if any should be taken to keep Cammell Laird in operation, at least for a limited period?

Costs

3. The additional costs of dividing the orders between the two yards are summarised in paragraph 9 of the note by officials. Ignoring the items in the comparison which roughly balance each other, there is an extra cost of some £47 million in the course recommended by Mr Heseltine (£7 million extra cost to the Ministry of Defence, an extra cost to BS of about £20 million for a cash injection to Cammell Laird and a loss of a further £20 million in reduced receipts from warshipbuilding privatisation).

x We £47 million for no net increase in jobs and £39,000 for each of the 1200 jobs transferred from Tyneside to Merseyside. Is this too high a price even to reward moderates?

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Arguments For and Against Splitting the Orders

4. Arguments in favour of giving one of the orders to Cammell Laird are:

- a. The good sense of the Cammell Laird workforce in overcoming industrial disruption deserves to be rewarded.
- b. The problems of Merseyside deserve special treatment.
- c. Cammell Laird should receive some benefit from having been the lowest tender in the first two tendering rounds. (Mr Heseltine is particularly critical of the fact that BS refused to allow Cammell Laird to tender for both orders on the third round, because redundancies there since last summer had deprived that yard of the capacity to build more than one vessel).

The counter-arguments in favour of Swan Hunter are -

- a. That yard's productivity and industrial relations record is substantially better than Cammell Laird's.
- b. Unemployment on Tyneside is now lower than on Merseyside. Protecting jobs on Merseyside through a Type 22 order would result in an exactly corresponding loss of jobs on Tyneside.

Responsibility for BS Additional Costs

5. If Cammell Laird were to receive one of the orders, Mr Tebbit is likely to argue that the Defence budget should be responsible not only for the total cost of the frigates, including any over-run, but also for the cash injections which would be needed at Cammell Laird (see paragraph 4 of his minute

of 21 December 1984). He will say that BS cannot be expected to bear the extra costs of the Cammell Laird cash injection within the very tight external financing limit in prospect for them.

Other Measures to Help Cammell Laird

6. The Ministry of Defence were earlier contemplating a major refit for the Balder London, which would have employed 300 people at Cammell Laird for a year at an extra cost (ie over and above the price to be expected through competitive tendering) of £2-3 million. They are not at present intending to go ahead with this, and have not been able to identify any further comparable work which, together with the Balder London, would make it possible to provide continuing employment for half the yard's projected workforce (500 redundancies are already in prospect out of the 1700 workers currently employed). Failing defence contracts, it might be possible for BS to secure sufficient civil work to keep the yard operating for another year, at the cost of an effective subsidy of £6-10 million. This would then provide an opportunity to sell the yard as a going concern, although this would almost certainly be more expensive than closing it down and then selling it as a facility without the workforce. If Cabinet agree that both orders should go to Swan Hunter, they may wish to ask the Department of Trade and Industry to consider urgently, together with the Ministry of Defence and the Treasury, what would be involved in securing sufficient work to keep Cammell Laird going for a further year and then selling it as a going concern (although not as a warshipbuilding yard).

HANDLING

7. You may like to invite the Secretary of State for Defence to speak first, since the substantive proposal before the Cabinet is that in his minute of 18 December 1984. The Secretary of State for the Environment will probably wish to



speak in his support. The Secretary of State for Trade and Industry, who has already made his views clear in his minute of 21 December 1984 could be asked to speak next. The Chief Secretary, Treasury will also wish to give his views about how the costs of the alternative courses might be met.

CONCLUSIONS

8. You will wish the Cabinet to reach conclusions on the following:
- a. the destination of the two Type 22 Frigate orders;
 - b. if one order goes to Cammell Laird, the responsibility for the resulting additional costs to BS;
 - c. if both orders go to Swan Hunter, possible alternative measures to keep Cammell Laird in operation pending its sale as a going concern.

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ROBERT ARMSTRONG

23 January 1985