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CEGB Network

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GOVERNMENT PRIVATISATION PROPOSALS

The attached statement to staff was agreed by the full CEGB Board at a special meeting on Friday 26 February.

You may find it useful to have the CEGB Board's response to the White Paper "Privatising Electricity".

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GOVERNMENT PRIVATISATION PROPOSALS

STATEMENT BY THE CEGB BOARD TO STAFF

1. The CEGB Board has now studied the White Paper putting forward the Government's proposals for restructuring and privatising the Electricity Supply Industry. We advise staff to study the White Paper themselves but the short summary dealing with those aspects of most concern to the CEGB, which is attached to this statement, may be helpful.

2. In formulating his proposals, the Secretary of State sought the advice of the CEGB, amongst many others, on what he should do. Before we responded, the Board made many studies of the issues. There were several meetings with the Secretary of State and his advisers, and the Board submitted many written papers. Our advice was based not on the preservation of the status quo but on careful analysis of what, in our judgement, would best serve electricity consumers. They want reliable electricity supplies - the assurance that electricity is always available at the flick of a switch whenever it is wanted - and prices which are as low as possible.

3. The main points of our advice were accordingly as follows:

- (i) To maintain reliability of electricity supplies, at lowest cost to the customer, the Grid and the bulk of the power stations should be kept together in a single command structure. Separation of transmission from main generation has not been attempted anywhere in the world. Because transmission lines do not act like a simple pipeline and because electricity consists of alternating current and voltage which must be controlled very precisely throughout the country, stability can only be achieved by an intimate collaboration between generating plant and the transmission system itself.
- (ii) The management of the integrated power system should have an obligation to supply electricity now and in the future, as a guarantee that the system as a whole would be planned, and new power stations ordered, so as to ensure the whole system was always ready to meet all the demands for electricity. This would continue to give clear accountability for security of supply. Under this obligation, the responsible organisation would have a natural reason to seek to build some nuclear power stations for strategic reasons, in particular to give diversity of fuel supplies, as well as for economic reasons.

(iii) Fragmentation of ownership of the existing power stations would increase the costs of electricity as a result of losing some of the demonstrable benefits of integration, such as the optimisation of fuel purchasing and distribution, maintenance scheduling, and holding of plant spares. If fragmentation were introduced, the power system would only continue to work effectively if the generating companies co-operated closely. Competition in the operation of existing capacity can only work if there is a substantial excess of plant for which the consumer would have to pay. The opportunity for real competition is in new capacity.

(iv) The best and most natural means of continuing with a nuclear programme which would benefit consumers would be to ensure that a large generating company retained the obligation to supply. Such a company would examine the case on its full merits. This was the way in which the Sizewell 'B' public inquiry was won, because the CEGB was able to advance the national case, and a positive decision was obtained only after the most thorough and searching public examination of all the issues - economic, strategic, environmental and safety. If no large generating company had the obligation to supply, no single corporate body could credibly advance the national case, leaving Government as the only other credible proponent. We did not advise the adoption of that alternative approach.

4. The CEGB also recognised the desire of the Government to introduce change and competition into the running of the electricity system. The Board shared these objectives. The CEGB accordingly proposed to Government a package with the following features:

- (i) All new capacity requirements should be put out to competitive tender, with the CEGB required to bid against other generators, We believed this would bring real competition from the outset, recognising that the nation faces a massive requirement for new power stations and that our discussions with interested groups over the last eighteen months have shown potential competitors do indeed exist. It would also give the Distribution Companies a much larger role in decisions about new capacity.
- (ii) Whilst operation of the Grid and the power stations should be under integrated management, the Grid could be put into a separate company jointly owned by CEGB and other users, including the Distribution Companies, to provide a guarantee of equality of access to the Grid by CEGB power stations and those of independent generators. Independent generators would then be able to bid for sales on the basis of commercial terms, rather than be compelled from the outset to enter the merit order and operate power stations at the instructions of Grid Control which would be an onerous and uncertain regime and might inhibit investment in the first place.

- (iii) Liberalisation of fuel purchasing, which holds out the prospect of very substantial benefits to customers.

The Board's case also rested on its excellent record of providing a secure and economical supply of electricity since we were formed thirty years ago. Despite having to use high cost British coal, electricity prices in England and Wales compare favourably with most other countries. We have also maintained a very high level of security of supply in both normal and adverse conditions. This has been achieved through the operation of our integrated power system with generation and transmission under a single command structure. The Board's proposals to Government were designed to build on those proven strengths and benefits of the existing system but also exploiting the further opportunities for cost saving which the introduction of competition could bring.

5. There are aspects of the Government's proposals which accord with the advice which we gave and which we can welcome:

- the undertaking that in future Generating Companies will be free to purchase coal and other fuels from the most competitive sources;
- the right of the Generating Companies to sell direct to large industrial consumers;
- the establishment of a commercial relationship between Generation and Distribution Companies, which means the end of the Bulk Supply Tariff and a greatly increased role for the Distribution Companies in planning new capacity;
- the transparency of the Grid, which opens it fully to new entrants into generation. (This could, however, have been more effectively achieved without transfer of day-to-day control of the Grid away from generators.) The same principle must apply to the lower voltage distribution system;
- the Government's undertaking that employees' rights and terms and conditions of employment will be safeguarded, and that wider career opportunities will arise;
- the proposals for high standards of service for customers.

6. Nevertheless, it is clear that overall the Government has rejected our advice, which was intended to work to the benefit of consumers. That is a profound disappointment. It is, however, a matter for the Government as to what advice it takes and to what decision it comes to. The Board of the CEBG has no right and no wish to frustrate the policies of an elected Government. The CEBG's assets are not "ours" to retain come what may, but are held by us on trust for the nation to deploy as Government and Parliament, determine. Similarly, the Government, through Parliament,

is entitled to determine new roles for us, the managers and staff of the CEGB. We may take pride in our record of 30 years of public service, in which we have consistently met our obligation to keep supplies flowing to the customer, in good times and bad. We must now look ahead to the new roles and the new duties which will develop. It is, therefore, our duty to take forward the new policy irrespective of our opinion as to its merits.

7. We accordingly now need to act on three fronts:
- (a) First, we must recognise that until Parliament enacts the Secretary of State's proposals, they do not change our responsibilities under the existing statutes to maintain a reliable and economic supply of bulk electricity. We need, despite all our disappointments and the uncertainties we face, to remember with some pride our record of public service and of achievement, and to continue to the best of our abilities with the task we all have to do.
 - (b) Second, in working up the details of the new arrangements, we must set ourselves the objective of trying to make the best of the proposals for electricity consumers.
 - (c) Third, we will want to ensure that the new companies are given the best possible opportunities to become, or contribute to, profitable energy enterprises, offering good business prospects to shareholders, exciting challenges to management, and good employment prospects to staff.

The extent and nature of the changes proposed, unprecedented in any electricity supply system in the world, will throw up some major challenges and problems. We note with approval that the Industry is to be fully consulted in the drawing up of the legislation and the subsequent re-organisation, and we shall deal with all these subsequent consultations and the issues arising, on their merits.

8. Throughout, we shall make it a point of great importance to have regard to the interests of staff. We note the Government's principle that "all who work in the Industry should be offered a direct stake in their future, new career opportunities and the freedom to manage their commercial affairs without interference from Government". Of course, it is much too early to comment on the detail of the proposals or to assess the future of the parts into which CEGB is to be split. We shall keep you informed as closely as possible as matters progress.

CEGB SUMMARY OF THE WHITE PAPER "PRIVATISING ELECTRICITY"
(Command 322)

1. The Government's intention to privatise the Electricity Supply Industry was included in its June 1987 Election Manifesto. The Secretary of State's main proposals can be summarised as follows:
 - (i) The 12 Area Boards are to be privatised separately as 12 Distribution Companies. They, and only they, will have a statutory obligation to maintain electricity supplies to consumers. They will be responsible for planning the provision of new power stations. They will have the power to order and operate their own power stations, subject to some restriction;
 - (ii) The Electricity Council is to be abolished;
 - (iii) The CEGB is to be split three ways:
 - The 400Kv and 275Kv grid, with its control centres, is to be hived off into, and operated by, a new company to be owned jointly by the 12 Distribution Companies. The Generating Companies will have no responsibility for or say in the management and control of the Grid, or the maintenance and development of the power system. This new transmission company will own and operate the Dinorwic and Ffestiniog pumped storage stations and the links with France and Scotland.
 - The CEGB's power stations are to be divided into two quite separate companies. The larger company, will own 70% of existing CEGB capacity including all the nuclear power stations. This company is the main successor to the CEGB. A smaller company is to own the remaining 30% of CEGB capacity. Which fossil stations go to which company is still to be determined. Neither of these companies is to have any duty to maintain electricity supplies. They cease to be public utilities and become energy companies.
 - (iv) All existing power stations will be needed to generate following privatisation. Contracts will therefore need to be agreed between the 12 Distribution Companies and two Generating Companies for the supply of electricity to the Distribution Companies. The Grid Company, acting for the Distributors, will call power stations up in a merit order but according to the contractual terms agreed. For new capacity, the Distribution Companies will have the ability to build their own power stations, or to contract with either of the Generating Companies or with any new Generating Companies that enter the market. The one important exception to

this is nuclear power stations. Here, the 12 Distribution Companies are to be obliged by law to contract for a specified minimum proportion of non fossil-fuelled generating capacity - in practice, this is likely to mean mostly nuclear plants. The proportion is not given in the White Paper, but will be specified by Government later. Nuclear power may in future come from any source, including Scotland and France.

2. It is intended that legislation to bring about these changes should be enacted in 1989, after which the 12 Distribution Companies, to which the Grid will be transferred, and the two Generating Companies will be offered for sale to the public, including the industry's employees.