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PRIME MINISTER

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THE FUTURE OF THE ROYAL DOCKYARDS

The MoD have worked up Peter Levene's proposal for contractorising the Royal Dockyards into a workable scheme. MoD are cautious about the benefits, but these could be substantial - perhaps £50 million off the £500 million cost of keeping the Navy seaworthy. The concept is not new. The Australian Navy has leased out a dockyard (At Cockatoo Island) for 50 years. Three points, in our view, deserve particular attention:

1. How should the redundancies aspect be best handled? Can, and should, MoD begin the task of slimming down the dockyards, prior to contractorisation in 1987?
2. How are the dockyards' assets to be managed, and accounted for?
3. What must MoD do to secure the advantages of commercial management?

Redundancies

The E(A) paper tells us that in the two years prior to contractorisation, the existing dockyard management would buy out restrictive practices (at £1,000 a worker), make 3,000 employees redundant, and improve efficiency by 10-15%. This

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would appear to give a better return than engaging contractors, according to the numbering in the paper, because it would avoid the need for additional contract staff and the contractors' profits. It would also avoid legislation.

In practice, the Dockyards Executive is unlikely to achieve this within a non-competitive, Civil Service framework. Dockyard managements should have their head on redundancies but should leave the buying-out of restrictive practices to contractors, who could probably do it more cheaply than MoD, if that is what is required. If MoD tries to do this, it may set a going rate, and create an expectation that there is one, for buying out the many restrictive practices in the dockyards.

Michael Heseltine is making heavy weather of the redundancy problem. He wants to organise a job creation programme because he thinks that dockyard skills would not otherwise find employment. MoD should concentrate on defence and leave DTI to handle this aspect, if they think it necessary at all. The dockyards' skills are marketable and the local unemployment rate at Devonport (13%), where most of the redundancies might occur is little higher than the national average.

It would be better to downplay the redundancies, and to say that the dockyards would be more competitive under commercial management and could attract work from outside MoD. The net effect on jobs cannot be certain: everything depends

on how the competitive the dockyards can become, with each other, with other British yards, and internationally.

Accounting for Dockyard Assets

The paper is unclear on this subject. The contractors must not have free use of the dockyard's £200 million assets. MoD predict, correctly in our view, that the contractors' charges will include a rate of return of 15% (£33 million) on these assets. MoD ought therefore to lease the assets on a commercial basis, and charge the contractors for any services provided. This will also insure that the contractors compete fairly with each other, and with other yards.

Securing the Savings

The Navy cannot expect to get the full advantage of these arrangements just by learning to write tight contracts for refit work. This itself is no easy task and an astute contractor might conceivably charge MoD more than the cost of the present, inefficient arrangements. Competition is the key to getting the savings. But MoD talk of opening only 10-20% of the workload to competition and offering "core programmes" to attract bidders. Why give these hostages when the Navy will be able to accurately predict only 15% or so of the four years refit programme when the bids for managing the yards are considered? There is scope for competition on 60% of the workload. The nuclear subs account for 40%. The SSBNs can

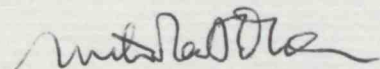
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only go to Rosyth, for technical reasons. SSNs and ships can be refitted at both yards, which should therefore be asked to compete with each other for this business. Michael Heseltine should be pressed to name a target share of the workload - perhaps 30% - to be open to competition.

Conclusion

We recommend that the proposals be fully endorsed, subject to the points above.


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