

CHAPTER 19

Conclusions

19.1. Our terms of reference require us to report whether the National Coal Board could, in relation to the development, production and supply of coal, improve its efficiency and thereby reduce its costs. We were asked to pay particular attention to operating costs, the system of internal cost control, purchasing policies, the methods of controlling stocks of stores and materials, the planning and appraisal of new investment, and the management, supervision and control of investment projects. As we have explained in Chapter 1, because our reference was limited to the development, production and supply of coal, our inquiry did not extend to other activities of the NCB.

19.2. The terms of reference do not require us to examine the NCB's pricing structure for coal, nor are we required to report whether the NCB is pursuing a course of conduct that operates against the public interest. We have therefore excluded consideration of these matters from our investigations and report.

19.3. In the preceding chapters we have examined the present position of the NCB and various aspects of its organisation and made a number of recommendations. For convenience, the major comments and recommendations are set out again at the end of this chapter. The effects of our recommendations, however, are likely to be limited unless certain fundamental problems are tackled. In the following paragraphs we discuss these fundamental problems, and make some suggestions and recommendations which may assist those responsible both in the coal industry and in the Government for the overall conduct of this industry. We also discuss (in paragraphs 19.29 to 19.37) certain questions of structure and organisation which did not fit conveniently into earlier sections of this report.

The position of the NCB

19.4. The coal industry has been very much reduced in size in the 36 years of the National Coal Board's existence, but the NCB remains by any standards a very large organisation. The performance of the coal industry affects the whole of the United Kingdom's economy, particularly through the influence of the price of coal on the price of electricity. About 80 per cent of electricity in the United Kingdom is at present generated in coal-fired plant, and coal represents 45 per cent of the Central Electricity Generating Board's costs.

19.5. Very large sums of public money have been needed to maintain the coal industry. The NCB has received regular and increasing support from the Government, including deficit grants to cover losses, and other grants for purposes including help in meeting the costs of the reduction of capacity. Grant aid receivable from the Government for 1981-82 amounted to no less than £575 million, which included a deficit grant of £428 million. The figures for the two previous years were £254 million (including deficit grant of £149 million) and £251 million (including deficit grant of £159 million) respectively.

19.6. In addition the NCB has borrowed substantially from the National Loans Fund and from other sources under Treasury Guarantee to finance the new and redeveloped capacity which the NCB has considered to be necessary to maintain the industry. In 1981–82 the NCB borrowed £902 million and in 1980–81 £586 million. The payment of interest on loans is now a major factor in the industry's need for deficit grants. The total interest charge amounted to £341 million in 1981–82. The figures for the two previous years were £256 million and £185 million respectively. The External Financing Limit (EFL) proposed for 1983–84¹, of £1,130 million, is easily the largest for any of the nationalised industries. Indeed it is over 40 per cent of the total for all these industries. On the information available to us, there is little possibility that the NCB will be able to operate without a deficit grant, let alone generate sufficient funds to finance any significant part of its own capital investment, before the end of this decade.

The objectives of the NCB

19.7. The Coal Industry Nationalisation Act, 1946, section 1(1), charges the NCB with the following duties:

- '(a) working and getting the coal in Great Britain, to the exclusion (save as in this Act provided) of any other person;
- (b) securing the efficient development of the coal-mining industry; and
- (c) making supplies of coal available, of such qualities and sizes, in such quantities and at such prices as may seem to them best calculated to further the public interest in all respects, including the avoidance of any undue or unreasonable preference or advantage.'

Section 1(4) of the Act provides:

'The policy of the Board shall be directed to securing, consistently with the proper discharge of their duties under subsection (1) of this section,—

- (a) the safety, health and welfare of persons in their employment;
- (b) the benefit of the practical knowledge and experience of such persons in the organisation and conduct of the operations in which they are employed;
- (c) that the revenues of the Board shall be not less than sufficient for meeting all their outgoings properly chargeable to revenue account ... on an average of good and bad years.'

19.8. It is to be observed that the policy required by sub-section (4) is to be pursued 'consistently with the proper discharge of [the NCB's] duties under sub-section (1)'. Parliament contemplated that the duties and the policy would be consistent with each other. The statutory statement of the objectives of the NCB is thus based on the assumption that the working of coal, the efficient development of the coal mining industry and the supply of coal as required by sub-section (1) are to be consistent with the policy prescribed in sub-section (4), in particular with the balancing of the revenues and the outgoings of the NCB on an average of good and bad years.

¹ Autumn Statement by HM Treasury November 1982.

19.9. The Plan for Coal of 1974 was intended to produce over 40 million tons of new and modernised capacity to meet the expected increase in demand and to offset the exhaustion of old capacity. There has in fact been no increase in demand and closures have taken place at a much lower rate than that envisaged. Nevertheless, until very recently the NCB has persisted with its development plans. We are concerned that these appear to have taken precedence over the statutory obligation to adopt a policy directed to securing that revenues shall not be less than sufficient for meeting all the outgoings properly chargeable to revenue account on an average of good and bad years. We have drawn attention in paragraph 9.111 to the circumstances in which much investment has gone into collieries which are either unprofitable or of doubtful profitability.

19.10. The NCB has told us that its general financial objectives for the present time are:

- (i) to seek to achieve an overall break-even after interest and social cost grants and without operating grants and achieve 50 per cent self-financing of investment as soon as practicable;
- (ii) to seek to meet this financial objective in a way which did not prejudice the progressive restructuring of the industry or its long-term capacity or efficiency; and
- (iii) not to regard the reduction of the requirements for external finance as a primary objective in the sense that it would override the two objectives above.

The NCB also told us that its aim was to meet as much of the potential demand in the United Kingdom for coal as it could meet economically. This, it explained, did not necessarily imply that it should always plan to meet the whole of the potential United Kingdom demand for coal.

19.11. The financial objectives set out in paragraph 19.10 are consistent with the requirements of section 1 of the Coal Industry Nationalisation Act, if social costs are regarded as not being 'properly chargeable to revenue account'. The help which Parliament has provided towards costs connected with pit closures and payments to redundant workers (see the Coal Industry Act, 1977, sections 6 and 7 as extended by the Coal Industry Acts of 1980 and 1982) shows that these social costs are not expected to be met entirely out of the ordinary revenues of the NCB. However, the financial position of the NCB at present is so difficult that, even with the help of social cost grants, the financial aim set out in section 1(4) of the Coal Industry Nationalisation Act is unlikely to be achieved for many years unless the highest importance is attached to economic production and production targets are set with due regard to the balance required between revenue and outgoings.

19.12. The NCB's present aim relating to output and demand (see paragraph 19.10) seems to us to be undesirably vague. It may be that if production targets were set as suggested in paragraph 19.11 they would be somewhat lower than forecasts of total United Kingdom demand. Whether higher levels of production, and so of capacity, are required for strategic or other reasons of

national policy is a question for the Government.¹ If the Government decides that such higher levels are required, the consequences should be determined by the Government and the NCB and form part of an understanding between them about the long-term plans for the industry. One result might be that the financial policy required by section 1(4)(c) of the Coal Industry Nationalisation Act would no longer be appropriate. If so, this consequence should be faced and a new policy requirement for the NCB should be defined by Parliament.

The problems of over-capacity and high cost pits

over capacity 19.13. The NCB is facing two crucially important problems, separate but closely related. They concern over-capacity and high cost pits. The first problem is that the NCB is producing much more coal than can find a market either in the United Kingdom or, at acceptable prices, abroad. As a result coal stocks held in the United Kingdom have been rising for a number of years, and in the NCB's own view are now excessive. These stocks are a continuing drain on the NCB's finances and a considerable burden on public funds. The second problem is that many collieries are being maintained in production although their unit operating costs greatly exceed the proceeds obtainable at present price levels in this country (at least £10 per tonne higher than current returns from exports), or at any reasonable estimates of future prices.

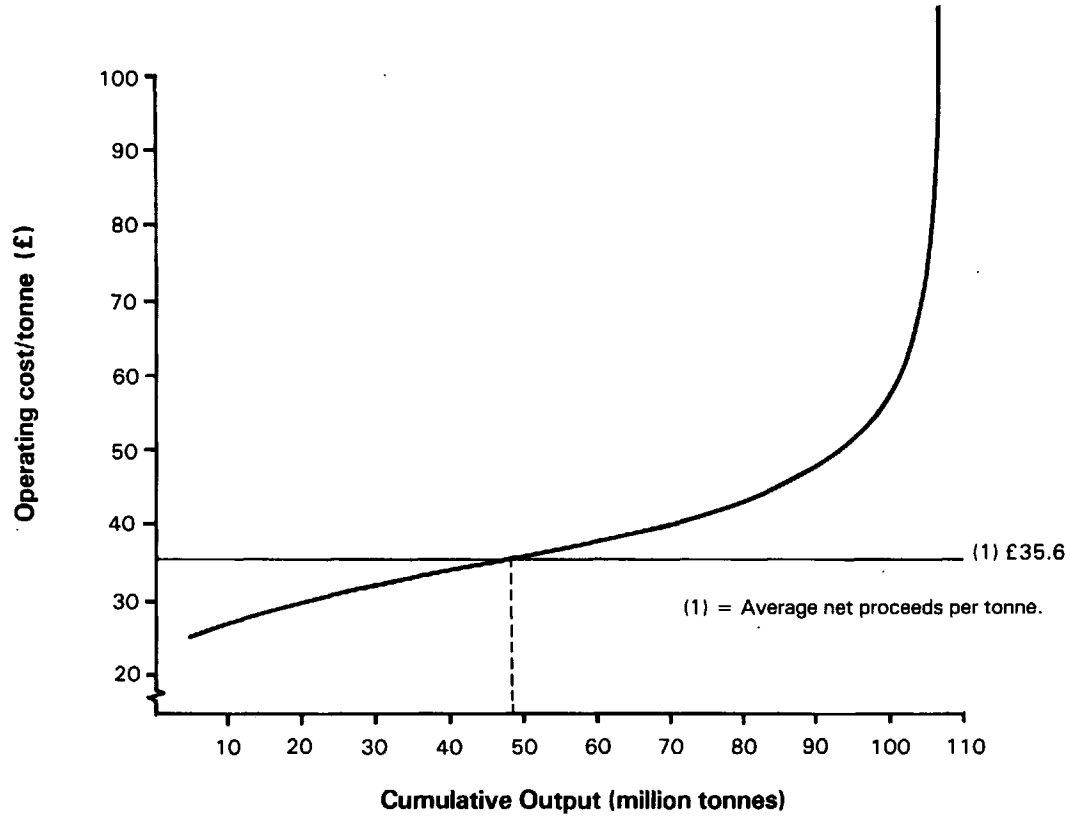
19.14. We have set out the background to the problem of over-supply in Chapters 5 and 7, and the facts in relation to the high cost pits in Chapters 3 and 8. The graph at Figure 19.1 illustrates the tail of high-cost capacity. It shows that well under half of the 1981-82 deep-mined output of 108 million tonnes was produced at levels of operating cost below current average proceeds. These average proceeds may be somewhat depressed, one reason being the need to dispose of coal in export markets at low prices, but Figure 19.1² shows that prices would have to rise very considerably to make much of the industry's high-cost capacity economic at present cost levels.

19.15. The high cost pits impose a heavy burden on the industry's finances. In 1981-82 the 10 per cent of the deep-mined output (10.8 million tonnes) that came from pits with the highest losses per tonne, involved operating losses of £263 million at average proceeds. Moreover, this is an understatement of the losses to the extent that 9 million tonnes were exported at a net realisation which was at least £10 per tonne less than the average home market price.

¹ See paragraph 28 of Second Report from the (House of Commons) Select Committee on Energy Session 1981-82: 'We reiterate our strong contention, already expressed in our Report on Industrial Energy Pricing Policy, that the cost of a decision which has more to do with social than energy policy should be borne on the appropriate Votes, which in this case would relate to employment protection or social programmes.'

² It does not follow that all collieries with costs lower than average proceeds make a surplus, or that all of those with higher costs make a loss. Some of the latter produce coal which commands a sufficient premium on the market to make a surplus, whereas some of the former produce lower grade coal selling at a low price. Moreover, collieries sometimes move into and out of surplus from one year to the next. Nevertheless, in general it can be said that for pits which are temporarily losing money there are others which are temporarily in surplus, and for those higher cost pits which are in surplus there are lower cost pits making a loss.

FIGURE 19.1 Deep-mined production: Unit operating costs against cumulative output, 1981-82



Source: MMC from NCB information.

19.16. We do not suggest that this capacity could be eliminated at one fell swoop, nor that the resultant savings could be fully realised immediately; savings would depend upon the phasing of closures, and substantial terminal costs have to be met in the year of closure and the years immediately following. The extent to which pits can be closed in any year involves difficult decisions and in making them the NCB has to take account of many different factors. The present position suggests, however, that problems of over-supply are likely to persist unless in course of time capacity can be reduced by about 10 per cent. Economic considerations, if taken alone, would indicate that the pits to be closed should be those with the highest unit operating losses per tonne but the selection of pits for closure has to take account of other factors. We cannot formulate any timetable or programme. We simply emphasise that any plan for the future of the coal industry must take account of the facts of the situation. Purely by way of example, we estimate that if capacity could be reduced by 10 per cent and the reduction could be concentrated on those pits with the largest operating losses per tonne, the NCB's finances would be improved to the tune of £300 million¹ per annum.

19.17. Further closures of high cost pits will, however, also be required when the investments of recent years bear fruit and new, economic capacity comes into production. This is a recurring feature of an extractive industry—collieries which have at one time operated successfully and profitably need to be closed and replaced by new mines when their economically extractable resources are exhausted. The industry's case for investment in new capacity cannot be sustained if it is unable to close down older, uneconomic units.

19.18. A significant reduction of the high cost tail of the industry would also be likely to enhance the NCB's efficiency in other ways. At present much of the time of senior management at Headquarters and Areas is taken up with the problems of high cost collieries. It is necessary to expend capital on development for production and on the maintenance of safety standards at all collieries regardless of their cost levels. Operating costs would be reduced if this finance and management effort were released, and some of it could be directed to the development of new mines, to the enlargement of existing capacity that would remain, and to the improvement of conditions generally.

19.19. We have examined the background to these problems to try to determine how the present situation has arisen. The current world economic situation, which has depressed world-wide demand for energy and perhaps retarded the expected move from oil to coal in industry, has clearly been a contributory factor in bringing about the over-supply position. However, the major reason for the over-production and the continued existence of so much high cost capacity, resulting in the present grave financial position of the NCB, has been the failure of the industry to achieve the elimination of 'a broad average of some 3-4 million tons capacity a year' that was accepted by the NCB, the unions and the Government, in the interim report of the Tripartite Coal Industry Examination in 1974. The other main element of that report—investment in new and modernised production facilities—has proceeded unabated. If the level of closure anticipated in the report had been

¹ This is made up of over £200 million operating losses (estimated at average prices) plus about £100 million benefit from not having to export at a discount.

achieved, present capacity would have been at least 10 million tonnes less than it is, and the position of the industry would have been transformed.

19.20. The need to solve these problems is not only of concern to the NCB. The Government has a major interest as the representative of the taxpayers who are providing support to the industry. The unions are also involved. They have a vital interest in the development of a modern and efficient coal industry. An industry smaller but secure is preferable to a larger industry with an uncertain future. Co-operation in a combined effort to secure a phased re-organisation of the deep mine capacity would be of the greatest benefit to the industry and to all who have a stake in its future. Such a re-organisation plan would involve commitments by all the interested parties to take the necessary steps for its implementation, including a renewed commitment by the Government to provide the necessary capital for development of the new and more efficient capacity that will be needed.

19.21. We recognise that the closure of high cost collieries would have serious implications for employment in some of the most depressed regions of Great Britain. This is a problem which cannot be avoided, for, in the absence of any practical means of significantly reducing the losses, many of the collieries in these regions cannot be kept open indefinitely. Mining industries, by their very nature, involve progressive closure of production in areas where the mineral can no longer be extracted economically. The social effects may be greatly alleviated by early retirement, by redundancy on the generous terms that are available (Appendix 8.1) and by transfers to continuing collieries. Where the social consequences of a decline in coal mining in a region would be particularly acute, it is for the Government to decide what action to take. This might be by the application of general regional policies (in particular to ensure that capital investment in new mines, or to extend the economic life of existing mines, attracts the same level of grants as would be available to other industries) or by the adoption of special measures in areas of special need.

19.22. The longer the problems are left the worse they will become. Unless there is a significant reduction of the numbers of high cost pits, the NCB's finances will deteriorate even further. The industry's ability to invest in modern capacity in the short and medium term will be jeopardised, for if the problem is not dealt with there must come a time when it will be quite impossible for any Government, faced with many calls on limited resources, to justify to the public the large and growing expenditure of public funds needed to continue support of high cost collieries. Action then, if the industry had been unable to invest in sufficient modern capacity, would be likely to be much more damaging than action taken now. In the meantime much taxpayers' money would have been committed and the price of coal might also have been kept higher than it need have been, unnecessarily increasing the cost of electricity to industry and thereby reducing the country's competitiveness in the world market.)

19.23. It would not be appropriate for us to define precisely the way in which the NCB should reduce excess capacity in high cost collieries. We do not attempt to specify by precisely how much capacity should be reduced, in what period the reduction should be made, or what individual collieries should be involved. It is for the Board to face the problem and take the necessary action.

The financial framework of the NCB

19.24. Our concern that in the past undue emphasis has been placed on production targets extends beyond the industry's objectives which we have discussed in preceding paragraphs of this chapter. We have found that the planning and management of existing deep mine Areas, collieries and formations are, except for the budget year and in the appraisal of new projects, mainly in physical rather than financial terms, eg tonnes of coal to be produced and manpower to be employed. Even in the budget year the financial targets and operating costs and profits do not take account of interest, and as the capital intensity of the industry rises, the 'operating profit' is becoming an increasingly misleading measure of financial viability. Interest costs at Selby, for example, are forecast by the NCB to be over one-third of total costs (Chapter 10, Table 10.2). The cost of coal eventually produced at Selby will be seriously understated unless interest costs on the capital that has been involved are included.

19.25. We have explained in Chapter 3 (paragraphs 3.125 to 3.130), that balance sheets are not prepared in any normal form at deep mine Areas or other formations. Profit and loss accounts do not include interest, there are no source and application of funds statements, and although unit costs include depreciation we understand that this is almost entirely confined to investment since 1974. There is therefore a lack of the necessary information that would enable the management to base its decisions on an understanding of the cost of the capital that is likely to be involved, or the real profitability or otherwise of individual operations.

19.26. The NCB has explained to us that there are difficulties in providing, even at Area level, adequate information to enable the balance sheets and other financial statements to be set up and maintained. It would want to retain the centralised operations of the Purchasing and Stores and Marketing Departments, and to avoid unnecessary administrative costs and management time in the allocation of, for instance, debtors and creditors. The NCB also told us, however, that, despite the difficulties, it was trying to achieve a better monitoring of the application of capital and capital productivity and had, this summer, taken steps to give Area plans a financial framework and financial objectives.

19.27. While we welcome the Board's general acceptance of the need for financial objectives and planning at Areas and other formations, we doubt whether the changes can be properly effective unless accompanied by changes in the organisation to provide management with balance sheets, profit and loss accounts which include interest, and source and application of funds statements identifying the cash flow of a particular unit. If this information is provided it will enable the Areas and other formations to be operated, for planning as well as day-to-day management purposes, as individual business units with financial as well as production targets.

19.28. We appreciate the nature of the difficulties in the way of providing the necessary financial framework for the changes we envisage, but they are of a kind that other organisations have successfully overcome. The operation of Areas and other major formations as business units will require individual

managers to have a much greater awareness of the cost of capital and the need to set and achieve financial targets as the most effective way of improving overall efficiency. We therefore recommend that the NCB should make the necessary changes to its accounting system and organisation to enable the deep mine Areas and other formations to have adequate financial information and to be operated, as far as is possible, as separate business units both for planning and for day-to-day management purposes.

The structure of the Board

19.29. During the course of our investigations we have discussed with the NCB the way in which its Board members carry out their corporate responsibilities. As will be seen from the description of the organisation in Chapter 2 (paragraphs 2.39 to 2.47), Board members do not have individual responsibilities for particular functions, although individual full-time Board members have been allocated Headquarters departments and other formations as 'special interests'. We understand that this type of interest is significantly different from a direct responsibility for the particular department. It would be possible to envisage a somewhat different organisation for the Board that would give individual Board members direct responsibility for certain major functions. We are told that the present system is well understood within the NCB so we do not consider that it would be appropriate at this time to make any recommendations for change in the style in which the members discharge their responsibilities. We have noted that the present full-time Board members are all former employees of the NCB, and with one exception all mining engineers. We consider that the Board would be strengthened if it included full-time members with a wider range of experience in industry and commerce. We therefore recommend that the Secretary of State should consider making a small number of appointments of this nature, even if in the short term it means an increase in the present numbers appointed to the Board, within the present statutory limit.

19.30. We have also discussed with the NCB the role of the part-time Board members. We understand that this role is at present under consideration as part of a general review of the role of part-time directors in nationalised industries. In these circumstances we have limited our enquiries to two aspects. First, we consider that in present conditions part-time members should be appointed from outside the industry. This recommendation is not intended as any criticism of the employee who is a part-time member at present, nor of other employees who have served on the Board. Our concern is simply that the Board should have the benefit of that diversity of background and experience which part-time membership makes possible. Our second concern is related to the role of the part-time members on the Audit Committee of the NCB. We have drawn attention in our report (Chapter 3, paragraphs 3.76 to 3.83) to the work of the Audit Department, and in Chapter 11 (paragraph 11.54) provided an example of the way in which the department monitors the efficiency of the NCB's activities. We consider that the work of this department is a valuable contribution to the efficiency of the NCB. We do not question its independence, but believe that this independence would be enhanced if the Audit Committee to which the department reports consisted only of the Board Chairman and the part-time Board members. Furthermore we recommend that, in order that the part-time members may make their experience available

to the Audit Department more frequently, the Audit Committee should meet at least four times a year.

The organisation of the NCB

19.31. The NCB told us that after the major review of its organisation in 1955,¹ and a major re-organisation of the deep mine Areas in 1967, its approach to organisational change had been evolutionary. Nevertheless in order to further the continuing ability of the industry to adapt flexibly to new circumstances, the Board had set up some time before our inquiry started an organisation planning group made up of a series of teams of senior managers. At present these teams are examining in particular the work of Headquarters departments. We were told that the emphasis of the teams' enquiries was so far essentially short to medium-term, with the initial aim of providing suggestions for more economic staffing. We were also told that the exercise had been designed in such a way as to offer at a later stage the further option of a longer-term look at the organisation to see whether organisational changes could contribute to more effective management and business decision-taking. The NCB told us, however, that until the problems of the immediate period had been dealt with, it did not consider it was opportune to undertake a major re-organisation of its structure.

19.32. We welcome the initiative of the NCB in setting up the organisation group and review teams and regret that the timescale of their operations prevented us from having the advantage of their findings. We appreciate the difficulties the industry is facing at the present time, but we do not think the Board can wait for the problems to be resolved before setting up the business units we have suggested, and considering and initiating any other necessary changes in its organisation to increase its efficiency. In the time available to us it has not been possible to consider fully the changes that may be necessary in the NCB's formations, but we have been able to examine some aspects of the organisation of the NCB Headquarters departments and deep mine Areas.

Headquarters departments

19.33. The staff at the NCB's Headquarters in London and Doncaster are organised in some 19 departments which advise the Board on all its activities and have functional links to non-Headquarters formations providing specialist services to the deep mining Areas, in some cases by outstationed regional organisations. Since there is no Chief Executive and the Board members do not have functional responsibilities, each department reports directly to the Board as a whole. The main departments (Finance, Mining, Industrial Relations, Purchasing and Stores, Staff and Marketing) are headed by Directors General who have a major role in advising the Board on policy matters. We noted that during the period of evolutionary organisational change there had been a tendency for the number of independent departments to grow, and questioned the NCB on the need for so many departments and the extent to which Board members to whom each was a 'special interest' are directly concerned with the activities of departments.

¹ Report of the Advisory Committee on Organisation (the Fleck Committee).

19.34. The NCB explained that the small departments, such as Road Transport, Estates Management, Public Relations, Legal, and European Community Affairs, take up little of the Board's time. Nevertheless, we are concerned that in an organisation where a small number of Board members are responsible for the overall direction and policy of a major industry so many departments should report directly to the Board. Furthermore the existence of so many separate departments may unnecessarily complicate the Headquarters organisation and increase staff costs. We therefore recommend that the Board should consider the amalgamation of a number of Headquarters departments.

19.35. It is appropriate to comment at this point on one aspect of the NCB management style. We have observed during our enquiries the tendency at all levels, in Headquarters and Areas, for the organisation to include a large number of committees. Where the committee is used excessively it can lead to a diffusion of responsibility, and to additional staff and administrative costs. We therefore recommend that the Board should examine the way in which it relies on committees in its organisation with the aim of reducing their use and introducing a greater degree of individual management responsibility.

The deep mine Areas

19.36. Since the major re-organisation of the deep mine Areas in 1967, the number of Areas has been slowly reduced as the number of collieries has fallen. At present there are 12 Areas of rather different size, ranging from the geographically larger coalfield Areas in the North-East, Wales and Scotland to the somewhat smaller Areas in the Midlands and Yorkshire covering the central coalfields. The NCB told us that, while it accepted that changes in the number of mines and the introduction of large mines such as Selby would require reconsideration of the present Area organisation, the Board had at present no long-term plans for change in the Area organisation. It would continue to make changes as and when it considered them to be necessary.

19.37. We believe that with the introduction of new capacity that is expected in the next few years, and the run-down of collieries in some Areas as they reach the end of their economic life, there is a clear requirement for the Board to plan well in advance for the necessary changes in the Area structure. Further, as we have explained in Chapter 15, we consider that there is a need for changes in the organisation of the workshops which are closely associated with the Areas. We also consider that the business units concept we have suggested in paragraph 19.28 is likely to be more effective if there is a restructuring of the Area organisation into larger units. We therefore recommend that the Board should review carefully its Area and workshop structure to take account of these factors.

Summary of major conclusions and recommendations from other chapters

19.38. Before we set out the major conclusions and recommendations from other chapters of the report it is necessary for us to explain that we appreciate that our inquiry took place at a time when the Board was having to consider major adjustments to its policies in the light of changing economic circumstances. The Board has not been able to make available to us before the date by which we are required to complete our report its latest development plan. We

have been told of a number of steps the Board is now taking to improve its procedures in many areas of activity, and have referred to these in our report. While we welcome these initiatives it will be obvious from what we have said that much more will need to be done. It was with these considerations in mind that we have framed our conclusions and recommendations, the most important of which from previous chapters are set out below.

Summary of conclusions and recommendations

| <i>Recommendation Number</i> | | <i>Paragraph Number</i> |
|------------------------------|--|-------------------------|
| Financial framework | <p>The NCB's budget process arises out of a dialogue between the Headquarters departments, deep mine Areas and other formations. There is a comprehensive system of financial budgetary control which is understood and operated satisfactorily throughout the industry. We note that a comparison of the financial results of the deep mine activity with budget shows that actual performance was close to budget over the last six year period. Net proceeds per tonne were 0.6 per cent better than budget, and total costs per tonne were contained within 1.6 per cent of budget.</p> | 3.131 |
| 1. | <p>Over the period 1976-77 to 1980-81 total unit operating costs per tonne rose for the deep mine activity by an average of 16.5 per cent per year compared with an average increase of 13.5 per cent in retail and wholesale prices, although in the most recent year 1981-82 unit operating costs moved approximately in line with inflation if social costs are excluded. We consider that the NCB should continue to impose the strict controls that have been applied in recent years so that the deep mine budget is set with the aim of reducing its unit operating costs in real terms in line with the increasing capital intensity of the industry. This will involve a maximisation of output from low-cost capacity with relatively low marginal costs and the reduction of the high-cost capacity.</p> | 3.132 |
| Demand forecasting | <p>Comparison of the forecasts made in past medium-term development plans with outturn shows that the errors in the estimates of total disposals of NCB coal are somewhat greater than the NCB might have expected. A large part of the error can be attributed to over-estimation of demand for coking coal. However, it is clear that until late 1977 the NCB was encouraged to plan coking coal production to match the BSC's expansion plans. As a result much investment was carried out, which, in the event, turned out not to be required. We do not believe that the NCB should be criticised for this; in such a situation it would have been very difficult for it to exercise independent judgment on the capacity to be provided.</p> | 4.70 |
| | <p>The NCB's forecasts of inland steam coal consumption have proved to be accurate, although this result arose from a combination of offsetting errors in key assumptions. However, these assumptions were not out of line with those that other forecasters in the field were making at the time.</p> | 4.71 |
| | | 4.72 |

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2. As regards demand in the year 2000 the latest NCB forecasts broadly agree with those made by other forecasters. However, despite the effort the NCB has put into investigating demand by the industrial sector we believe that the uncertainty attached to the forecasts of industrial consumption is greater than that attached to other parts of the forecast. **We therefore recommend that great caution be exercised by the NCB in its appraisal of capacity designed to meet this market.** 4.73
- In recent years the NCB has changed from producing a central forecast of demand to producing demand scenarios in an attempt to examine the uncertainty that surrounds the forecasts. **We welcome this change in emphasis.** 4.74
3. One of the major purposes of examining the future is to estimate the price at which future output from investment should be valued. The demand scenarios, recognising that there is potential competition from imported coal, are constructed on the assumption that the price ruling in the United Kingdom will be set by prices on the world market plus transport charges. The NCB does not at present estimate how its share of the home market would change if it charged a premium over world prices, nor by how much its prices would have to be cut to supply a larger volume of export customers. **In view of the sensitivity of the rate of return on investment to the price realised for coal we recommend that in its planning the NCB should investigate the consequences for its sales of varying the price of its product relative to world market prices.** 4.75
4. While we understand why the NCB has lately been selling coal overseas at prices which do little more than cover the short-run avoidable costs of production, **We do not consider that over the longer term it should continue to rely on such low price sales for reducing surpluses of coal.** 4.76
- Long-term planning** The NCB's longer-term planning has been deficient in a number of important respects: 5.71
- (a) The MTDPs and the succeeding Development Plan to 1990 have only been projections of a few major indicators such as production, average costs and average prices used to support the NCB's requests for revenue subventions and capital finance from the Government, and have not related to any specific performance targets required from operating formations by the NCB. As such, the plans have not lent themselves to monitoring for control purposes.
 - (b) Although the plans have been designed to support the NCB's submissions for investment finance, they have not permitted assessment of whether funds provided in the past have been well spent nor have they provided estimates of the return promised on new capital.
 - (c) Because the plans have shown only aggregates of production, sales, cash flow and so forth they have not drawn attention to the major problems currently facing the NCB, particularly heavy losses on a long tail of high-cost collieries and over-supply.

- (d) The plans have not demonstrated the robustness of the NCB's chosen course to different levels of demand, differences in the trends of the NCB's costs relative to international prices and to different trends in operational efficiency.

As regards the fourth point, we welcome the introduction of alternative demand scenarios in the Development Plan to 1990 and the NCB's expressed intention as regards future development plans to test the robustness of its plan against alternative demand scenarios.

We have examined the NCB's recent longer-term plans and have noted that they are drawn up at Headquarters using considerable data input from operating formations. We make the case in Chapter 7 for the preparation by each Area and other operating formations of business plans covering the budget and four ensuing years. **We consider the business plans should be consistent with the objectives set out in the longer-term plans produced at Headquarters.**

5.72

5.

The main lesson we draw from the NCB's difficulty in reducing supply and bringing it into balance with demand is that it should henceforth adopt a much more cautious approach to investment intended to increase or maintain production capacity, at least until such time as it is fully satisfied that it will be able to eliminate high-cost excess capacity.

5.74

**Cost structure
and performance
trends in
deep mining**

Unit production costs have been increasing in real terms. The main component of this is the increase in unit wage and wage related costs.

6.52

Over the period 1969-70 to 1981-82 there has been, especially since 1977, a steady improvement in labour productivity at the face and on the surface. These improvements have been offset by a steady decline in labour productivity elsewhere below ground so that the improvement on overall productivity has been only 9 per cent.

6.53

The modest rise in labour productivity has been the result of a combination of actions:

6.54

- (a) Capital investment in face and surface machinery.
- (b) Redistribution of output in favour of those production units with higher OMS. This includes the effects of closures, mergers and investment in new capacity.
- (c) Implementation of an incentive scheme.

These actions were offset by the adverse ageing effect of continuing capacity which is an inherent characteristic of the mining industry, and represents an overall effective reduction in productivity of at least 0.75 per cent per year.

**Performance
measures**

The NCB's principal measure of performance is a measure of labour productivity defined in terms of saleable output of coal in tonnes per man-shift worked. The measure is used at both local management and Area planning levels. It is backed up by a large range of associated measures in terms of work category and contributing factors. The scope of the labour productivity measures at the operational management level is adequate for normal control of operations.

6.55

| <i>Recommendation Number</i> | | <i>Paragraph Number</i> |
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| 6. | We recommend that the NCB should review the nature and structure of its performance measures, in order to achieve a balanced monitoring of the use of all resources and their unit costs linked to a set of commercially orientated measures. In particular they should properly reflect all costs including the cost of capital. The NCB should also give consideration to devising a measure or measures of the productivity of capital which properly reflect its true value. The capital measures should monitor both productive and non-productive assets, at least down to Area level. | 6.58 |
| The planning and control of deep-mined coal production | [<i>Text omitted. See note on page iv.</i>]] Area Directors do formulate what the NCB calls 'strategies' for their Areas. These are not quantified in terms of the resulting effect on Areas' costs or profits, or in terms of the time by which they should be accomplished. | 7.124 |
| 7. | We recommend that the NCB should go further and develop a formal system of national and Area business planning covering the next five years ahead including the budget year. | 7.125 |
| 8. | We recommend that within the framework of such a planning system the Board should define clearly how it intends to achieve the presently projected productivity growth and set out the various intended measures in a way suitable for subsequent monitoring. | 7.128 |
| | The NCB has controlled the numbers of face and surface industrial staff better than the numbers of craftsmen and industrial staff elsewhere below ground. The NCB is conscious of the need to take specific action in these areas and has already had some success. More needs to be done, however, and we recommend that in any new planning system high priority should be given to developing targets for reduction in the numbers of craftsmen and all employees who work elsewhere below ground. Targets should be sufficiently quantified to allow proper monitoring of their achievement. | 7.129 |
| 9. | We have noted in paragraph 7.111 that it is normal for the NCB to keep both national and Area man-shift budgets fixed over the budget year, even though it may become clear during the course of the year that the circumstances have changed, and that further savings could be made. We therefore recommend that manpower and man-shift budgets should in future be varied during the course of a year if advantage could be taken of trends in absenteeism and wastage as they become apparent. | 7.130 |
| 10. | International comparisons | 7.73, 7.81 Appendix 7.1 |
| | We asked two of our technical advisers to carry out a comparison of mining efficiency in Great Britain and the Federal Republic of Germany. The report concludes that the productive efficiency of the modernised coal faces studied in British mines is not significantly different from that on comparable coal faces at similar modern mines in the Federal Republic of Germany. | |
| Investment and investment appraisal | In our assessment of the NCB's investment programme we noted that over one-third of the Board's expenditure on large major projects has gone into collieries which are either unprofitable or of doubtful potential profitability. On this basis we consider that the Board's investment programme has not fully met one of its major objectives, namely restruc- | 9.105 to 9.111 |

turing the industry by investment in potentially profitable collieries. As a result of our examination of its appraisal procedures and its investment programme, we have made a number of observations and recommendations which we consider will enable the Board to appraise more thoroughly investment proposals. We set these out in the order in which they appear in the chapter.

- | | | |
|---|---|---------------|
| 11. | (a) The NCB agreed that it should consider amalgamating the two systems of colliery classification and adopt a more stringent interpretation of the financial criteria adopted in classifying collieries for delegation of authority purposes. | 9.60 |
| 12. | (b) The NCB should revise its appraisal procedures to ensure that: <ul style="list-style-type: none"> (i) the minimal feasible alternative is selected as the base case; (ii) investments to which closure is the alternative are carefully appraised; and (iii) the Department of Energy is informed of components of very large projects which are not expected to earn an adequate return after risk. | 9.74 |
| 13. | (c) The NCB should introduce a separate risk analysis of market-related factors for projects at existing collieries and should adopt a consistent treatment of its appraisal of all major projects according to a range of possible market outcomes. The NCB should also reconsider its practice of applying, in the case of new mining projects, a trend of rising colliery net income over an extended period. | 9.77 to 9.79 |
| 14. | (d) The NCB should analyse its project performance with a view to achieving a more realistic Stage II prospectus and it should make allowance in the financial appraisal for the likely shortfall in performance. We also recommend that remedial action should concentrate on Areas which consistently fail to achieve their investment objectives. | 9.93 |
| 15. | (e) In its appraisal documents, the NCB should consider the marginal yield of the project and the potential profitability of the colliery in separate sections. | 9.94 |
| 16. | (f) The NCB should extend the appraisal of the plant pool programme to include life-cycle costing. | 9.97, 9.98 |
| 17. | (g) The NCB should develop a formal system for allocating its investment funds according to the contributions which projects promise to make towards the attainment of the Board's financial targets. For example, selection should be based on the prospective marginal return of projects. It should consider bringing forward the Stage II submissions in the cycle of project appraisal (or determining the relevant financial information earlier) in order that the ranking of projects can be based on reliable information. | 9.99 to 9.104 |
| The management of major projects | We found that not all of the NCB's contractors employed on major construction projects made available critical path analysis networks although the NCB tried to persuade contractors to produce them. We think it would be beneficial | 10.18, 10.19 |

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18. for the NCB to have this important management tool available for all major projects and it is unsatisfactory to have to obtain them by persuasion. **We recommend that the NCB should make it a condition of letting a contract that contractors are required, in cases where the project manager considers it to be appropriate, to provide critical path networks.**
19. We believe that the use of computer packages could be beneficial to the NCB's project management. **We recommend that the NCB investigate the packages now available with the intention of introducing them in all cases where the management of a project could be made more effective by their use.** 10.21
20. We refer to the lack of immediate effective action when successive annual reports on a project at Oakdale colliery in Wales indicated a serious deterioration in the expected results. The reports were seen by the Headquarters Review and Project Committees which are responsible for advising on remedial action. We consider that in the circumstances there should at least have been a reappraisal of the project to consider whether it should continue or if changes were required. **We recommend that the Board take action to ensure that its Headquarters review procedures are more rigorously applied.** 10.42, 10.43
- Information provided by the NCB indicates that 36 (47 per cent) of the 77 large major projects completed by the end of December 1981 were delayed by more than one year and the average delay was 14 months. 10.43
- We note that the NCB has introduced detailed changes into its control of investment projects. On the basis of the criticisms we have made we would, in the absence of the changes that the NCB has introduced, have recommended that the NCB should undertake a thoroughgoing review of its system of progressing and controlling investment projects. It is too early to say whether the changes introduced by the NCB will be sufficient to deal with the problem of project delays. **If in two years' time investment projects continue to show discrepancies between forecast and actual completion times we consider that such a review should then be carried out with the intention of investigating the reasons for the delays and introducing a revised, comprehensive and up-to-date system incorporating appropriate modern methods and techniques, and taking full account of the lessons learned from the implementation of our recommendations in paragraph 10.21.** 10.45
21. The current instructions on project management date from as early as 1957 and are not all contained in one document; **we recommend that a comprehensive manual incorporating the changes that have been made and setting out the Board's policy and requirements with regard to the management of investment projects be compiled and issued to all appropriate staff.** 10.60
22. At present the overall control of all projects, including Selby, is vested in the appropriate Area Director. **We consider that there would be advantage in the case of the largest greenfield sites, where the ultimate responsibility for the success of the project must lie with the Board, for project management to be the responsibility of an individual manager accountable directly to the Board.** 10.61
23. 10.86

| <i>Recommendation Number</i> | | <i>Paragraph Number</i> |
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| 24. | In general we found that the NCB's contract practices in respect of major construction projects were satisfactory and should help it to obtain competitive prices. | 10.96 |
| Opencast Executive | We were glad to note that the Opencast Executive is now limiting single tender action but we were concerned that no direct steps are taken in single tender contracts to check the level of profit made by the contractor. We recommend that in the case of single tender action taken in respect of the extension of an existing site the contractor should be required to make available details of the level of profitability of the existing site. | 11.90 |
| 25. | | 11.91 |
| 26. | We refer in paragraph 11.54 to quantities of coal recovered from a site over and above the contractual tonnage, for which prices have to be negotiated with the contractor. One category of such coal is known as excess coal. We recommend that where there is an unusually large amount of excess coal, the contractor should be obliged to make available, in the negotiation on the price to be paid for this excess coal, details of the profits he was making from the site on the basis of the contract quantity. | 11.92 |
| 27. | We suggested to the NCB that the system of tender invitations from a select list might not always give the Opencast Executive the best bargain. The NCB drew our attention to a number of potential difficulties in open tendering, but we consider that the supposed value of restricted tendering has not been demonstrated. We therefore recommend that experiments with open tendering should be conducted in a few contracts in each Region so that the advantages and disadvantages can be evaluated. | 11.93 |
| 28. | The operations of the licensed opencast operators produce about 5 per cent of the total British opencast output—some 700,000 tonnes out of 14 or 15 million tonnes—and many of them sell the coal they produce in competition with the NCB. We consider that this provides a small but valuable element of competition to and comparison with the operations of the Opencast Executive and should be encouraged as a means of increasing the efficiency of the NCB operation. Moreover, the techniques used in opencast operations have developed considerably since the present statutory limit on the operations of the licensed operators was fixed in 1958. We recommend therefore that this should be increased to a new limit of 100,000 tonnes, and that there should be provision for appeal by the operator to the Secretary of State if the Executive refused to grant a licence for a site containing a quantity of coal within the statutory limit. These changes would require legislation. | 11.95 |
| Industrial wages | We refer in Chapter 19 to the desirability of NCB Areas and other formations being treated as business units. The Opencast Executive would lend itself to this treatment which, <i>inter alia</i> , would enable a realistic return on capital employed to be established. | 11.96 |
| | Wages constitute almost one-third of the NCB's total operating costs. Increases in wages tend to flow through to wages charges. (For definition of wages charges see paragraph 3.37.) The totality of wages costs is thus about one-half of the NCB's operating expenditure and (as noted in paragraph 3.37) real wages costs per tonne, although fluctuating from year to year, have shown a long-term tendency | 13.49 |

to rise. **In these circumstances it is of special importance that the NCB does everything in its power to control wage costs and avoid unreasonable increases.**

We have noted that in spite of increasing operating deficits and mounting stockpiles of unsold coal, and against a background of reduced recruitment needs and a decline in natural manpower wastage, mineworkers' earnings have continued to increase relative to those of workers in most other industries. We have no doubt that this is a reflection of the collective bargaining pressures in the industry. Nevertheless we are not satisfied that the industry's financial and economic positions have been accurately reflected in the agreements reached in recent years.

13.50

We have noted the progress which the NCB and the unions have made over the years in reforming the wages system. In particular the incentive scheme has been effective in rewarding effort and boosting productivity especially at coal faces. We note too the comprehensiveness of the NCB's wage monitoring and control systems and its efforts to prevent earnings 'drift' under the incentive scheme, ie increases beyond those which can be attributed to actual improved performance or increases in the standard incentive rate. **We recommend that the NCB should continue to pay close attention to this aspect of the scheme and in particular that it should ensure that standards are reassessed promptly when there are significant (favourable or unfavourable) changes in geological conditions.**

13.51

29.

**Non-industrial
staff**

In relation to the scale of mining activity (and in some respects in absolute terms) the size of the NCB non-industrial workforce continues to grow. We appreciate that some of the increase may be due to the concentration of production in larger mines and the use of more sophisticated technology. Additionally we note that the NCB has cut staff numbers substantially during the last two years, and has set up review groups to examine the costs and staffing of Head-quarters departments. We consider it to be of great importance that the NCB continues with its efforts to limit the number of non-industrial staff to what is necessary for its operations.

14.54

Accordingly we recommend the following:

30.

(a) **The NCB should continue to establish forward objectives for reductions in all levels of non-industrial staff and take the necessary steps to achieve them.**

14.55

31.

(b) **The NCB should move towards a position where the decision to carry out clerical work study or other functional surveys of non-industrial work, including that of technical and management staff, is taken centrally, as part of regular reviews of all parts of the organisation as well as at the request of formations.**

32.

(c) **The NCB should consider establishing a centrally directed Management Services Unit which would incorporate the Methods Evaluation Unit and bring together different aspects of NCB services affecting the control of staff numbers and the introduction of new methods. The new Unit should report to the Board's Committee on Cost Savings.**

33. (d) **The size and coverage of the Methods Evaluation Unit should be increased and an effort should be made to recruit people to the Unit who have relevant experience in other industries.**
34. (e) **A quantitative study should be carried out to ascertain whether the rest and contingency allowances applied to clerical work standards are appropriate to the circumstances.**

We recommend that:

35. (a) **The NCB should reconsider its policy on recruitment of staff with experience of other industries, with a view to securing as much openness of its career structure as possible.** 14.56
36. (b) **The NCB should make fuller use of available information relating to remuneration in other industries in general (not just the energy sector). The objective should be that while a proper regard for internal relativities in relation to supervisory relationships and career progression should continue to play a part in salary determination, market remuneration levels in relation to skills and qualifications, together with ability to pay, should in future have a much greater weight.**
- The use and repair of mining machinery in the NCB** Plant is hired out to pits on a charging basis fixed by each Area according to individual circumstances, but though it is supposedly aimed to recover the costs of plant used no charge for interest is included. The high cost in both revenue and capital terms of ensuring adequate plant availability (some £140 million revenue and £150 million capital per annum) demands close management control. We believe that this can best be achieved if the plant pool system is operated as a series of largely self-contained business units which are required to have proper regard to the cost of capital employed. 15.8
37. The NCB is examining the possibility of life-cycle costing, a technique which seeks to optimise the total overall costs of plant and machinery. We recommend that the NCB give a high priority to this examination with a view to early implementation. 15.22
38. The NCB has 26 Central Workshops of widely varying size, with an annual turnover of £215 million employing 9,000 industrial and 600 non-industrial personnel. We consider that 26 workshops is too large a number to service the needs of the industry efficiently and economically. They are not located to best effect, and there is duplication of facilities. 15.33
- We appreciate that there are industrial relations factors and social costs to be considered, and that any substantial reorganisation could involve additional transport costs and problems of access to collieries. We are glad to note that the NCB has sought to rearrange some of the product ranges overhauled by individual workshops. However, we do not believe this goes far enough, and we recommend that the NCB should investigate the possibilities and the costs and benefits of rationalising the workshops' structure. 15.35
39. **The NCB should investigate the possibilities and the costs and benefits of rationalising the workshops' structure.**

| <i>Recommendation Number</i> | | <i>Paragraph Number</i> |
|---|---|-----------------------------|
| Purchasing and Stores Department | The NCB allocates about a third of its national contracts by number, and three-quarters by value, on other than a least cost basis. In view of the extra immediate costs involved in allocating contracts on other than a least cost basis, not only in the prices paid but also in administration, we are concerned that the procedure should be used only when it can be fully justified. We accordingly recommend that the procedures for monitoring Purchasing and Stores (P & S) Department decisions on such allocated contracts should be strengthened. | 16.27 |
| 40. | | 16.99 |
| 41. | We recommend that the NCB should take more effective measures to expedite the establishment of standards for all items for which it can be shown to be cost-effective and should consider the temporary augmentation of the Standardisation Unit possibly by use of contract staff or by the employment of a mining consultancy. | 16.100 |
| 42. | The NCB's computer-based stock control system is wide-ranging and impressive but has a number of unusual features. Reviews of the effectiveness of some aspects of the system are now being carried out. We recommend that the reviews should pay particular attention to the features we have identified with a view to incorporating suitable modifications to the computer models if this can be done economically. This would reduce the need for manual intervention. | 16.101 |
| 43. | Half of the demands on Central Stores comes from Central Workshops. In order to ensure that materials are available to meet the workshop programmes, the programmes are set out for six to nine months ahead and rolled forward monthly. Variations from former trends in the usage of parts are identified and through a time-consuming 'scaling' process changes are made to the forward annual demand. Computer developments are already under way to eliminate the labour-intensive aspects of this process with a view to applying material requirement planning (MRP) principles to the ordering of the high value turnover items. This will be a significant step forward but we believe it would be advantageous to apply these principles to all items, the usage of which can be scheduled in advance by the workshops. | 16.102 |
| 44. | P & S Department costs increased by some 20 per cent in real terms between 1973-74 and 1980-81. The reasons given for this increase include the cost of computer programming and operations which have not been fully offset by savings in other areas. The NCB told us that staff numbers fell rapidly in 1981-82 and the trend is continuing into 1982-83 and beyond. However, the NCB considers that more significant savings have flowed from stock reduction of some £80 million which it states has been achieved without lowering service totals (paragraph 16.96). We believe it is difficult to identify how much of the stock savings, and the financing cost savings to which they have given rise, can be directly ascribed to the benefits of the computer system, although we fully recognise the importance of capital costs in this area. In view of the real increase in the revenue costs of the P & S operation we recommend that particular attention should be directed towards monitoring these costs in future. | 16.105 |

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- It has not been possible to establish the total cost of the purchasing and stores activities, partly because of the absence of any account of the cost of capital employed in these activities and partly because these activities at Area and colliery levels are not separately costed and budgeted.
45. **In order to establish the overall performance of the P & S activity we recommend that both the revenue and capital costs of these operations at Area and colliery levels should be separately budgeted and monitored.**
- Estate management** The NCB has been successful in disposing of a large proportion of its stock of houses at a capital benefit of £100 million net between 1972-73 and 1981-82 inclusive. It still possesses over 41,000 houses, many of which are let at rents below the registered fair rent level. 17.16
46. **We commend the Board's policies of disposing of as many houses as possible and of reducing the burden of its inherited obligations by bringing the rents of the houses that remain in its possession up to registered fair rent levels as soon as it is practicable.** 17.12
- We are concerned that the level of administration and management costs incurred by Coal Industries Estates Ltd in respect of the NCB's farms and estates appears to be a much higher proportion of the income than we should expect. We appreciate that overall the rents may, justifiably, be lower than the average for the country as a whole and that the NCB's costs may include elements which would not be covered in a normal commercial agreement. Nevertheless we recommend that the Board should examine the level of CIE's administration and management costs and include in this examination an evaluation of the possibility of using agents, at least for some of the work, as an alternative to directly employed staff. 17.23
47. **Nevertheless we recommend that the Board should examine the level of CIE's administration and management costs and include in this examination an evaluation of the possibility of using agents, at least for some of the work, as an alternative to directly employed staff.**
- We are also concerned about the apparent lack of any incentive for the Estates Department to optimise its land management operations, and of any yardstick against which it may be judged except the simple profit and loss accounts. 17.24
48. **We appreciate that land transactions are to some extent unpredictable, but we recommend that the department should be given as realistic as possible a profit target each year and be held to account for its performance.**

J G LE QUESNE (*Chairman*)

A D BAÏN

H L G GIBSON

R L MARSHALL

C M MILES

J S SADLER

N E D BURTON (*Secretary*)

26 November 1982

