Soviet Union

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Ref. A01477

PRIME MINISTER

CEGB Uranium Enrichment Contract with the Soviet Union

(OD(80) 12)

on Afghanistan Sit^n

When OD discussed Afghanistan on 22nd January, one of the conclusions put forward by the Foreign and Commonwealth Secretary was that "we should pursue the political and economic measures directed at the Soviet Union which we have been discussing in NATO ....". As a result the Secretary of State for Energy raised with the Foreign and Commonwealth Secretary the question of the Central Electricity Generating Board's contract with the Soviet Union for uranium enrichment. This involves sending uranium hexafluoride from this country to Russia to be processed and returned as enriched uranium to fuel nuclear power stations. You asked for the matter to be considered by OD. The Secretary of State for Energy has therefore been invited, and has tabled OD(80) 12 which recommends allowing the contract to stand. Other invitees are the Secretary of State for Scotland (because the contract also involves the Scottish public utilities) and the Attorney General.

HANDLING

2. You will wish to ask the Secretary of State for Energy to introduce his paper; and the Foreign Secretary to comment on the implications for our policy towards the Soviet Union post-Afghanistan.

3. The points to establish in subsequent discussion are:-

(a) Can the Government actually order the CEGB to cancel the contract? The letter attached to the Secretary of State for Energy's note suggests that the CEGB would not resist any Government action to terminate the contract provided that a clear event of "force majeure" could be brought about, but the letter also suggests that this would be very difficult to achieve. What is the position?

Mr Pl 6 → [illegible] → CEGB

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(b) If the CEGB does agree to cancel the contract, what are the likely penalties? Could the CEGB be sued successfully for damages in the Soviet courts and to what extent might the Government need to compensate CEGB for any damages?

(c) What are the alternative sources of supply? What extra costs would be involved in having to make use of them?

(d) What is the particular nature of the Scottish Office interest in this issue? It is not clear whether the Scottish interest is different in principle from that of England and Wales.

(e) What are the West Germans doing about their similar contract? The answer is almost certainly nothing, because West Germany public utilities are partly in private ownership, and because this particular contract forms part of a wider network of energy contracts (particularly for natural gas) which West Germany has got with the Eastern bloc.

(f) How exposed to criticism will the Government be, particularly from the United States, if this contract continues? It seems likely that this contract will attract public notice only if an attempt is made to cancel it.

CONCLUSIONS

4. In the light of discussion on these points the Committee might be guided to reach the conclusion that the contract should be allowed to stand, because it is a long standing one, because the Germans are not cancelling theirs, because cancellation might make the Government liable for considerable damages, and because the Board's enriched uranium needs could only be met from other sources at considerable extra cost. The decision is needed urgently because the first shipment of uranium hexafluoride is due to leave this country for the Soviet Union this month.

RTA

(Robert Armstrong)

20th February, 1980

DEPARTMENT OF TRADE 1 VICTORIA STREET LONDON SW1H 0ET Telephone 01-215 7877

From the Secretary of State

NBPM

Ruth

CONFIDENTIAL

The Rt Hon The Lord Carrington KCMG MC
Secretary of State for Foreign and
Commonwealth Affairs
Foreign and Commonwealth Office
Downing Street
London, SW1A 2AL

20 February 1980

Dear Peter.

CEGB URANIUM ENRICHMENT CONTRACT WITH THE SOVIET UNION

Unfortunately I will not be able to attend the OD discussion on Thursday but I have seen the note by David Howell (OD(8012) and I should like to support the conclusion in his letter to you of 8 February that this contract should go ahead. The practical considerations are important here but I would also like to emphasise the trade policy aspects which suggest that cancellation would be damaging in principle as well as practice. These aspects were of course set out in the letter sent by Cecil Parkinson's Private Secretary to David Howell's on 25 January.

I am copying this to the Prime Minister, David Howell, George Younger and Sir Robert Armstrong.

Yours ever
John.

JOHN NOTT

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Soviet Union

SCOTTISH OFFICE
WHITEHALL, LONDON SW1A 2AU

The Rt Hon David Howell MP
Secretary of State for Energy
Thames House South
LONDON
SW1P 4QJ

13 February 1980

CONFIDENTIAL

Dear David

CEGB URANIUM ENRICHMENT CONTRACT WITH THE SOVIET UNION

Thank you for sending me a copy of your letter of 8 February to Peter Carrington.

It is clear that we can reasonably intervene to have the CEGB contract cancelled only if we are certain that such action would satisfy the force majeure provisions of the contract. Your letter raises serious doubts on this score, suggests that trade in nuclear materials could be prejudiced to BNFL's overall disadvantage, and refers to the possibility that CEGB and SSEB would seek compensation from the Government. In all the circumstances I am inclined to agree with your conclusion that the contract should be allowed to continue.

I am copying this letter to the recipients of yours.

GEORGE YOUNGER

MR. ALEXANDER

The Prime Minister has suggested that this should be discussed at E. OD might be more appropriate, and she will accept this.

Cabinet Office have suggested an ad hoc meeting. They say no OD is scheduled. I told them that one will have to be scheduled for the Arab/Israel paper, and that we should decide tomorrow whether this subject can be added. Another ad hoc meeting is unnecessarily messy at present.

MAP

11 February 1980

How long does the contract last?

Prime Minister

(2)

SECRETARY OF STATE FOR ENERGY
THAMES HOUSE SOUTH
MILLBANK LONDON SW1P 4QJ
211 6402

8/2

We should discuss this M

The Rt Hon The Lord Carrington KCMG MC
Foreign and Commonwealth Secretary
Downing Street
London SW1A 2AL

8 February 1980

Dear Peter

CEGB URANIUM ENRICHMENT CONTRACT WITH THE SOVIET UNION

Following your minute of 25 January and letters from the offices of George Younger and Cecil Parkinson, my officials have discussed this matter with the CEGB and with BNFL.

Briefly, achieving effective cancellation of the contract without penalty could well be impossible, and the benefits to BNFL of getting the work from the CEGB either directly or through Urenco could well be outweighed by disadvantages to them in losing other business for the conversion of uranium hexafluoride (UF6) and its onward transport to the USSR.

The contract between the CEGB (contracting on their own behalf and on behalf of the SSEB) and Technabexport makes no provision for cancellation on notice. The contract can therefore only be lawfully cancelled, without giving rise to a possible claim for damagesfor its breach, under its force majeure clause. This provides that if circumstances beyond the control of the parties make it impossible for either party to perform its obligations under the contract, the time for performance shall be extended while the parties try to find a solution which will make fulfilment of their obligations possible. If however the circumstances continue for more than 12 months, the contract may be cancelled without liability to pay compensation. Import and export prohibitions are included as examples of force majeure.

The export of UF6 is subject to export licence. If the Government were to refuse an export licence for shipments for the purpose of fulfilling this contract, it would be open to the Russians under the clause described above to ask the CEGB to divert one of their incoming shipments of natural uranium to the USSR for conversion and enrichment there or, less likely, to offer to provide UF6 from their own resources for the purpose of fulfilling the contract. If they did either of these things, there would be no basis for cancellation of the contract.

The import of enriched uranium is subject to import licence. But, the CEGB are contractually obliged to pay for enriched uranium as soon as it is loaded on to a ship in a Soviet port. Refusal of an import licence would not frustrate the contract.

Thought has been given to the possibility of using exchange control legislation (even though presently dormant) in this case, to prevent the CEGB making payment, but there is legal advice to the effect that there is considerable doubt whether a Court would regard this as constituting force majeure for breach of contract.

It therefore seems that it may well be impossible for the Government to bring about a clear event of force majeure. It is understood that the contract, though providing for arbitration in Sweden, is written under Soviet law, so that if force majeure were not clearly established, the CEGB could be sued for damages in the Soviet Courts.

If a way could be found of cancelling the contract lawfully, we would expect the CEGB to look to BNFL or Urenco for replacement quantities of separative work.

why?

BNFL could only do it for more than twice the Soviet price. If the work went to Urenco, BNFL would only get a third of the benefit. Urenco's price for doing the work would, even on the basis of some element of discount, be likely to be at least $25 per swu more than the Soviet price. This would mean an extra cost to the Boards of about £10m over the life of the contract. It is relevant that BNFL engage in conversion of uranium oxide to UF6 on behalf of European utilities and then ship it to the USSR for enrichment. They are at present negotiating further contracts for work of this nature worth some £20m. The cancellation of the CEGB contract, in which they are involved through their responsibilities for converting the uranium oxide into UF6, could well cause the Russians to refuse to undertake further business involving BNFL in this capacity. BNFL believe that the benefit foregone in this way would more than offset what they would expect to gain if the CEGB has to come to Urenco for replacement quantities. Because of the wide price differential, they would not expect the CEGB to come to them, or, if they did, for the full amount. The benefit to BNFL is hence small (through Urenco) or speculative (on their own). There would also be long term affects on BNFL's reputation as a reliable supplier.

It is my officials' impression that the CEGB would not resist any Government action to terminate the contract, provided that a clear event of force majeure could be brought about and that there was no possibility of their having damages awarded against them. They have said however that in the event of cancellation they would want to be free to seek the most advantageous terms available elsewhere, including France and the US. Although we would wish to prevent their doing this, it throws further doubt on the benefit to BNFL of cancelling the Soviet contract. The Boards might seek compensation from the Government.

It is for you and John Nott to form a view about the effects on Anglo-Soviet trade and on Anglo-Soviet relations of trying to break this contract. From my officials' talks with those involved, it seems that the difficulties of doing so are great, the benefits so far as trade in nuclear materials is concerned are dubious and the likelihood of a

frustrated legal wrangle in which the Generating Boards might suffer financially through a Soviet court decision is considerable. So far as my own responsibilities are concerned, I now tend to think that the contract should be allowed to continue, but I should be glad to know urgently whether you agree. The urgency arises from the fact that the first shipment of UF6 under the contract could be required to leave the UK before the end of this month, and would have to leave BNFL's Springfield works several days before the planned departure of the ship.

I am copying this letter to the Prime Minister, to John Nott, George Younger and Sir Robert Armstrong.

Yours ever

David

D A R Howell

Soviet Union

Prime Minister

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FCS/80/14

SECRETARY OF STATE FOR ENERGY

Trade with the Soviet Union

1. You wrote to me on 21 January about the CEGB's contract with the Soviet Union for enrichment of uranium. I was surprised to learn that the CEGB had gone to the Russians in the first place, given that security of supply could in due course be brought into question for political reasons. I understand, however, that the decision was taken for reasons of price and because of a possible shortage of enrichment services which was then foreseen.

2. In normal circumstances the arguments against government intervention in trade for political reasons are strong. Even after the Russian invasion of Afghanistan it is not our wish to restrict trade with the Soviet Union where there is clear advantage to British firms. However, in the light of the more aggressive Soviet attitude to relations with the West, it seems to me sensible not to give the Russians levers which they could use against us. On these grounds I should be in favour of transferring CEGB's contract away from the Russians.

3. The overall commercial advantage to the UK also appears on balance to favour cancellation of the Russian contract and its replacement by an arrangement with URENCO. I understand that the CEGB have no strong feeling either way. As you point out, there is a risk that the Russians would retaliate against other British firms by deliberately switching business away from them. I doubt, however, that cancellation of the CEGB contract would add significantly to the chances of Soviet retaliation, given the action we are already taking against them in the fields of credit and technology following the invasion of Afghanistan.

4. On balance, therefore, I would favour cancellation of the contract on government instructions, and am content for you to hold discussions with the interested parties as you propose.

4. I am sending copies of this minute to the Prime Minister, John Nott and George Younger.

(CARRINGTON)

Foreign and Commonwealth Office
25 January 1980

2 pps

SCOTTISH OFFICE
WHITEHALL, LONDON SW1A 2AU

The Rt Hon David Howell MP
Secretary of State for Energy
Thames House South
Millbank
London
SW1P 4QJ

25 January 1980

NBR? yet

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TRADE WITH THE SOVIET UNION

I have now seen a copy of your letter of 21 January to Peter Carrington about the possibility of our requiring CEGB to break its contract with the Soviet Union for uranium enrichment work.

The case for asking the Boards to withdraw from the contract is, in my view, fairly strong. Withdrawal would, I understand, seem not to be likely to create serious difficulties for SSEB provided that it followed direct and unmistakable Government intervention so that the "force majeure" provision in the contract can be brought into play. At the very least, I think that we should ask for the postponement of the proposed visit to Moscow by the CEGB delegation, on which, incidentally, SSEB is not to be represented, to enable the arguments for and against intervention to be considered at greater leisure.

In the time available I have not been able to give any consideration to the question of the availability of alternative supplies of enriched uranium. I should be grateful, therefore, if you would arrange for your officials to keep mine closely in touch with discussions on this matter so that SSEB's interests, which may not necessarily coincide with those of CEGB, can be fully taken into account.

I am copying this letter to the recipients of yours.

Approved by the Secretary of State
and signed in his absence

DEPARTMENT OF TRADE
1 VICTORIA STREET
LONDON SW1H OET
TELEPHONE DIRECT LINE 01 215 5146
SWITCHBOARD 01 215 7877

From the
Minister for Trade 's office

NBPI

The Private Secretary to
the Secretary of State for Energy
Department of Energy
Thames House South
Millbank
London
SW1

25 January 1980

Dear Private Secretary,

TRADE WITH THE SOVIET UNION

You copied your Secretary of State's letter of 21 January to Lord Carrington about the CEGB's contract for the enrichment of uranium to the Secretary of State for Trade who is at present in the Far East. Our copy of the letter arrived only yesterday afternoon.

Mr Parkinson saw the letter before he left for his constituency. In his view it is unfortunate that we are being pressed at such short notice to take a decision that could have serious consequences for Anglo-Soviet trade relations. He is concerned about the possible damaging effect of cancellation of this contract on the prospects for UK companies. Coming so close on the heels of the announcement of the sanctions against the Soviet Union this action could so easily be regarded as a sign that UK companies in general - the Soviet Union will not necessarily attach much importance to the CEGB's status as a nationalised industry - are going to renege on their contracts and take their trade elsewhere.

In the energy sector alone UK companies have a considerable amount at stake. The International Offshore Consortium (Wimpey, Brown & Root and BP) is in the final stages of negotiation for the oil fabrication yard on the Caspian Sea. This contract even in its recent more restricted form is still worth about £85m. There are many other good prospects, particularly in the offshore oil and gas sectors, where UK companies have considerable experience and expertise to sell.

The sort of action that is contemplated goes beyond what Ministers have agreed should be the present scope of sanctions against the Soviet Union. Collective Ministerial decisions entail no attempt to interfere with normal trade. And on the measures that have been taken by the Community to withdraw subsidies there has been no disturbance of existing contractual obligations. It is not clear from your Secretary of State's letter whether we are at a point of no return and a crucial decision on cancellation in relation to this contract has to be taken before the CEGB party go to the Soviet Union on Monday. If

it does, my Minister considers that in terms of the existing collective decisions, that decision must be not to intervene. If it were possible, postponement of the CEGB visit would allow time for more careful consideration of the issues involved.

I am copying this letter to the Private Secretaries to the Prime Minister, the Foreign Secretary and the Secretary of State for Scotland.

Yours sincerely,

Vivien Thackeray

VIVIEN THACKERAY
Private Secretary to the Minister
for Trade (CECIL PARKINSON)

Soviet Union

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(2)

SECRETARY OF STATE FOR ENERGY
THAMES HOUSE SOUTH
MILLBANK LONDON SW1P 4QJ

Tel: 211 6402

Prime Minister
This is relevant to OD tomorrow. A good candidate for cancellation on the face of it.

The Rt Hon The Lord Carrington KCMG MC
Secretary of State for Foreign Affairs
Foreign and Commonwealth Office
Downing Street
London SW1A 2AL

21 January 1980

21/1

Dear Peter

TRADE WITH THE SOVIET UNION

We have been considering the relations of our nationalised industries with the Soviet Union. The CEGB have a contract with the Soviet Union, concluded in 1974/75 and known to the former Government, under which the USSR will enrich substantial quantities of uranium for the CEGB. The contract is for the supply of 1000 tonnes of separative work, starting this year and continuing until 1989. The total contract is worth some £50m to the Russians. Uranium hexafluoride will be shipped from here to Russia and returned as enriched uranium, about 90-100 tonnes at a time. The first shipment of uranium hexafluoride is due to leave here in March; before that happens, a CEGB delegation (with an SSEB representative) has to go to Moscow for final negotiations dealing with the interpretation of the price clauses in the contract. They are due to travel on 28 January. The enriched uranium is for use in AGR nuclear power stations: it will amount to about 20% of CEGB's annual supplies.

To direct the CEGB to break this contract would be a major act of policy, and decisions on this must rest on the balance of advantage between foreign policy and commercial considerations. I understand that a Government direction to break the contract would get the CEGB out without penalty, (although it is always open to the Russians to sue in the UK courts for breach of contract). Urenco should be able to supply the services instead, and BNFL as the UK partner in collaboration could gain a substantial share of the business as a result. There would however be some price disadvantage for the CEGB, as Urenco supplies would be more expensive. However, they would also be secure. Implementation of the contract could also be delayed without penalty by Government direction, provided this is sufficiently clear and public to convince an outside body such as the London Chamber of Commerce.

There appear to be three possible options:

i. cancellation of the contract on Government instructions

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ii. notification to the Russians of a delay of 1 year in its implementation: and a review of the situation in say, 6 months time.

iii. non-interference in the contract.

Cancellation would involve interfering with the CEGB's commercial judgement. It could have commercial advantages for BNFL, but disadvantages for other UK companies trading in the Soviet Union. In the final analysis, the decision will need to be taken in the context of our overall relations with the Soviet Union.

I should like to know if you think that consideration should be given to including cancellation of this contract in any package of economic sanctions against Russia that is drawn up in response to the invasion of Afghanistan.

I should be grateful to have your views and those of John Nott and George Younger, to whom I am copying this letter. We need to decide quickly whether this is an option we want to pursue; if so officials will need to discuss it immediately with interested parties including CEGB, SSEB, and BNFL and Urenco.

I am also copying this letter to the Prime Minister.

Yours ever

David

D A R HOWELL