

From: "Vadera, Shriti" <Shriti.Vadera@hm-treasury.gsi.gov.uk>  
 To: "Dan Corry" <Dan.Corry@dtlr.gsi.gov.uk>, "Vadera, Shriti" <Shriti.Vadera@hm-treasury.gsi.gov.uk>, "zzNO10\_Adonis, Andrew" <AAdonis@no10.x.gsi.gov.uk>  
 Date: 29/08/01 10:19:10  
 Subject: RE: Ariel

1. we can talk to David about transition management - I discussed it with him early on and this is one I get the feeling he has grasped the nettle on - I think he is waiting for an offer from the ubiquitous Bechtel. I think the ideal for us would be to get Robinson support but squeals from others so we get a nice balance of not endorsing the management but looking sensible and at the same time announcing the interim changes which would include a contract with Bechtel and others to enhance existing management

2. I'm afraid I totally disagree with Andrew's view on giving control to the TOCs. We should rehearse the arguments before hand to get a common line as I do not think it would be a good idea for us to disagree publicly in front of the team today as they are already all over the place without us adding to the confusion. I think we will go a long way to meet the fragmentation concerns - see Mercers section when it arrives - but giving the TOCs "control" is not in our best interests in terms of service, deliverability or vfm - not to mention it is inconsistent with the not for profit model as TOCs are thinly capitalised equity profiteers of the worst kind. No all the critics are not wrong about this being a problem - it does not mean they have the right solution having not done analysis/had access to data and can we please remember we are being lobbied by those who have most to gain by TOC control - they may not all be wrong but they sure as hell are all acting in their own best interests

I think you are over sceptical about getting the Ariel structure right - I think it needs some concentrated brain power on this issue which has been notably lacking from the team. I am considering bringing in PUK to help on the contractual arrangements and structures for a non profit co as I think a lot of the incentives will derive from PFI style (not the same though) contracts from the trust to the industry. What do you think?

3. I think it would politically dreadful to be paying off Ariel shareholders and I see absolutely no reason we should want to. There is no point in worrying about it now as it will be something that comes out of the administrator's negotiations and valuation not for us to make an offer. The important thing for us is - in a UNITED way - to give the clear view that we do not think it is for the Government to bail them out and our position is (not to mention Ariel's own advisers') that there is no value left in the equity. If we start with a weak signal your prophecy will be self fulfilling. I do not think this is one for us to wobble on - we have enough things to spend money on in the sector without worrying about bailing out shareholders who added no value to the company

-----Original Message-----

From: Dan Corry [mailto:Dan.Corry@dtlr.gsi.gov.uk]  
 Sent: 29 August 2001 09:42  
 To: Shriti.Vadera@hm-treasury.gsi.gov.uk; AAdonis@no10.x.gsi.gov.uk  
 Subject: RE: Ariel

I'm also concerned about the transition in terms of management. I presume that ideally we want Robinson and the top brass to stay a bit. He might be up for it if we sorted it with him in advance. But we cannot tell him this in advance as it would put him in an impossible position vis a vis shareholders. So we will not know if he will paly ball until we have done the deed. Which means we need a fallback in case he walks.

>>> Andrew Adonis <AAdonis@no10.x.gsi.gov.uk> 08/29/01 07:58am >>>  
 Agreed - the more I think about this, the more it seems to me that without some significant measure of vertical integration in the arrangements for the New Ariel, the management (as opposed to the financial) case for such a drastic change is almost impossible to make. But with it the debate is transformed because (a) if we get the New Ariel structure right (a big if) this gives us a credible reason for believing and arguing that we can

eliminate the blame culture and improve management quality radically by giving the TOCs and others in the industry a compelling interest in the quality of Ariel's management and performance, (b) because it makes it far easier to slim down the regulation significantly; and (c) because vertical integration is the near universal demand of the serious critics (who can't all be wrong).

But of course we need a credible model for New Ariel which the TOCs are prepared to buy into - without being able to negotiate with them in advance. My instinct is that we could get away with announcing 'a significant (or controlling?? - a v important issue) stake for the TOCs in the management and governance of New Ariel, on which we will conduct intensive consultations with them in the coming weeks' - but only if we have a working model of our own which we are satisfied with.

I'm also worried about the shareholder compensation issue. Whatever the formal value, and the reliability of the procedure for assessing it, how realistic is it in practice to give them nothing or virtually nothing?

-----Original Message-----

From: Vadera, Shriti [mailto:Shriti.Vadera@hm-treasury.gsi.gov.uk]  
Sent: 28 August 2001 19:08  
To: 'Dan.Corry@dtfr.gsi.gov.uk'; zzNO10\_Adonis, Andrew  
Subject: Ariel

<<Project Ariel.doc>> As discussed outline of things SoS may want to say to ensure that officials minds are focussed on the specificity we need. I hear the Mercer report is going to contain good things on vertical integration so the message seems to have got through and I can put in more specifics after it arrives. If you think it would help we should circulate tomorrow - if you agree let me have comments

While drafting this I came to the conclusion this could increase not decrease the pressure on LU - it has obvious similarities to K arguments including TOCs/LU Opsco doing maintenance and lack of risk transfer while the difference are vital but subtle and less easy to explain succinctly

Meeting has moved to 4 - we should consider chatting together before then

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