



House of Commons
Trade and Industry Committee

**Success and failure in
the UK car
manufacturing
industry: Government
Response to the
Committee's Fourth
Report of Session
2006–07**

**Third Special Report of
Session 2006–07**

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The Trade and Industry Committee

The Trade and Industry Committee is appointed by the House of Commons to examine the expenditure, administration, and policy of the Department of Trade and Industry.

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Second Special Report

The Committee published its Fourth Report of Session 2006-07 on 29 March 2007.¹ The Government's response was received on 18 May 2007 and is published as an Appendix to this Report.²

Government response

Introduction

The Government welcomes the Committee's report on the UK automotive manufacturing sector which presents a balanced assessment of the key issues relating to the future of automotive manufacturing in the UK. It has been particularly useful to have the Committee's views to help with the development of Government policy in this area as we strive to ensure the success and sustainability of this important industry in a challenging global environment.

Responses to Conclusions and Recommendations

Below we have set out our responses to those conclusions and recommendations directed at Government where we believe it is appropriate for Government to respond. The conclusions and recommendations are numbered as they appear in the report.

Future of the UK car manufacturing industry

1. Like our predecessors we see mixed prospects for companies manufacturing passenger cars in this country, and for individual plants. There were particular reasons why Longbridge and Ryton closed and for the loss of the third shift at Ellesmere Port. However, though the combination of problems experienced by these plants may have been especially acute, we heard nothing to make us believe that they were unique to these plants or their parent companies. It is therefore all the more important that both the industry and Government put extra effort into improving skill sets throughout the sector, increasing the commitment to R&D, adopting lean manufacturing techniques and strengthening the local supply chain. (Paragraph 85)

Government agrees with the Committee that the challenges faced by the UK automotive industry in maintaining global competitiveness are around skills, business processes, the efficiency of the supply chain and constant investment in R&D. The Government also believes that the UK automotive industry is well placed to succeed. Recent excellent news such as the decision by General Motors to build the 'New Astra' at Ellesmere Port from 2009 in the face of stiff European competition, and Toyota's decision to build a foundry for engine production in Deeside, shows that the UK industry is in good shape.

1 Fourth Report from the Trade and Industry Committee, Session 2006-07, *Success and failure in the UK car manufacturing industry*, printed as HC 399 on 29 March 2007

2 The Paragraphs in bold type are quotations from the list of Conclusions and Recommendations in the Committee's Report.

But we cannot be complacent. The areas identified by the Committee for extra effort are those highlighted for action by the Automotive Innovation and Growth Team (AIGT) in 2002, reaffirming that Government and industry efforts are focused on the right issues.

As indicated in the Government's written and oral evidence to the Committee's Inquiry on "The Future of UK Manufacturing: Skills Shortages", we accept the need to actively address skills issues through a wide range of activities. The Committee acknowledges the important role played by the Automotive Academy. Work to improve automotive-focused skills will continue through the recently launched successor—the National Skills Academy for Manufacturing (NSAM).

We are committed to supporting innovation and the introduction of new automotive technologies. The Energy Review announced the development of the Low Carbon Transport Innovation Strategy (LCTIS) and the Energy White Paper will shortly be published giving details of a new Low Carbon Vehicle Innovation Platform. The recent Budget Statement also announced a review of new technologies which could help decarbonise road transport over the next 25 years (see Recommendation 8 for further details).

The Supply Chain Groups programme includes automotive sector projects. According to the latest assessment, this approach has made significant improvements in quality and delivery performances at virtually every host and supplier under the twelve projects reviewed. Returns show productivity improvements of 30–40%, with many companies at the second and third tier level being exposed to the tools and techniques of process improvement for the first time.

A competitiveness analysis of the Japanese component manufacturers who invest in the UK is underway which will help our understanding of their current challenges and how we can support their future success. We anticipate that this study may also be useful in terms of improving the supply chain more generally.

The Government recently announced the extension of the Manufacturing Advisory Service (MAS) to support the development of lean manufacturing techniques further. The new phase of MAS—to be launched in April 2008—will offer an extended range of help and advice to small and medium sized manufacturers—covering, for instance, strategic planning and skills development, and improving the performance and operation of the supply chain.

In addition to these initiatives, we will be giving consideration over the coming months to the merits and timeliness of updating the work of the AIGT and taking a new strategic forward look at the automotive industry in the UK over the next 15 to 20 years.

The automotive industry is of massive importance for jobs, growth and prosperity in the UK and we remain committed to doing everything we can to help ensure the sector has a successful future here.

Worldwide automotive industry

2. At present the automotive industry still seems to be wedded to a regional approach to its markets, expanding or contracting capacity to meet regional demand. Logistical costs and the need to reflect local tastes are important factors in limiting the scope for supplying customers from plants outside the region. While we do not believe that a shift in production from Western Europe to the cheaper Asian economies is imminent, like our predecessors we believe that the closure of car plants in Western Europe and the opening of up-to-date facilities in Eastern Europe, using cheaper labour, will continue. (Paragraph 12)

We agree that the success of Eastern Europe in attracting inward investment is likely to continue in the short to medium term. There are suggestions that the ‘low cost’ advantage of producers in this region is beginning to erode as wage inflation takes hold but we recognise that, in turn, new low cost regions will emerge elsewhere. Ultimately, the plants that survive will be the ones with a strong focus on cost management and, crucially, with the right products for the market. Demand for UK-made vehicles and parts is robust and with a strong partnership between Industry and Government, the UK automotive industry should have a solid future ahead.

The recent investment decisions by Toyota and General Motors have demonstrated that UK remains a competitive manufacturing location for automotive products, thanks to our competitive labour market, and an ability to adapt to new challenges; in addition to the natural advantage of proximity to a substantial UK and European customer base. When taking account of the full cost of moving manufacture to ‘low cost’ countries, many companies are finding that a comprehensive analysis of cost, quality and timely delivery renders the UK as the best place to manufacture their products.

As the Committee will be aware from the Department's submission to its current inquiry into the future of UK manufacturing, the Government is taking action through its Manufacturing Strategy to encourage the development of a strong, high value added manufacturing sector with the ability to compete successfully in world markets.

Factors affecting individual plants

3. Unsurprisingly, the age of plants influences decisions on which factories to run down or close where there is over-production. However, it is not simply the case that if a facility is old, it will close. Some companies have invested large sums of money in developing and upgrading factories—for example, neither BMW's Cowley plant nor Ford's Dagenham one is a new facility on a greenfield site. It is also arguable that, after more than 20 years of operation, Nissan's factory in Sunderland is hardly “new” Of more importance than simple age is the degree to which plants are capable of adaptation to modern manufacturing equipment and practices, and the cost of adapting them relative to building or upgrading facilities elsewhere. (Paragraph 20)

Government agrees with the Committee's assessment that competitiveness depends on a wide range of factors. For instance, manufacturing the right products for which there is a demand is critical to success—without this no amount of investment will render any plant viable; whatever its age. As Ellesmere Port has recently shown, even long

established UK car plants can still win investment against the stiffest of competition and here, the UK's success can be directly attributed to industry's capacity and willingness to adapt to change.

This flexible approach is fundamental if plants are to succeed in securing new investment. Of course, Government support is vital. This can include financial support. In the period 2000–2006, some £100 million was offered in regional grants under the Regional Selective Assistance (RSA) and Selective Financial Investment in England (SFIE) schemes to automotive manufacturers and suppliers in England. In the same period, nearly £150 million was paid out, including stage payments on offers made prior to 2000. Government will continue to consider applications for grants under the SFIE product for businesses that are looking at the possibility of investing in an Assisted Area and need financial help to go ahead—including existing businesses that wish to expand, modernise or rationalise activities.

4. It is clear that the logistical models adopted by GM and PSA have contributed to the cost disadvantages faced by Ellesmere Port and Ryton. However, other car companies are also importing significant proportions of their components and exporting most of their finished products, while still managing to manufacture profitably in the UK. (Paragraph 28)

Clearly it is not for Government to comment on any company's logistical model. This is a commercial matter. Each plant is different, and the balance of which parts to make locally and which to buy in, can vary considerably depending on how a company manages its logistics. The logistics model employed by PSA at Ryton was only one factor in the plant's closure.

Ellesmere Port was one of five European plants competing for the next-generation 'New Astra' model. The plant's management, Trades Unions and workforce, together with Government and the local agencies, worked co-operatively to ensure that Ellesmere Port was in the very best competitive position. Great gains have been made at Ellesmere Port over the last eighteen months and—as noted above—on 17 April, GM Vauxhall announced that the UK site had succeeded in its bid to produce the New Astra, thereby securing the longer term future of the plant.

5. We were surprised to learn that PSA considered labour costs higher in the UK than in France. We recommend that the Government study this potentially significant claim to see whether there is such an incentive to cut manufacturing jobs in the UK, and we would like to be informed of the Government's conclusions. We are also concerned about the more predictable labour cost disadvantage vis-à-vis Eastern Europe. We have recently started an inquiry into the impact on UK business of the recent expansion of the EU to Eastern and Central Europe, and intend to consider, amongst other things, the synergies that UK companies could achieve through working better with their equivalents in Eastern Europe. (Paragraph 31)

We agree that it is important to try to gain a better understanding of the implications of wider social costs on UK competitiveness and, in this respect, the Government will be interested to see the conclusions of the Committee's inquiry into the impact of the expansion of the European Union on UK businesses. Competitive threats clearly exist,

but there are also major opportunities in this growing part of the European regional market, which UKTI is actively promoting to relevant UK companies.

In consideration of labour costs alone, data show these *are* higher than in France, but lower than in some other EU-15 competitors, such as Germany, and the USA. In 2004 (latest data available), the normalised hourly wage of production workers in the motor vehicle and parts manufacturing industry were:

Czech Republic	22%
Italy	74%
France	90%
UK	100%
USA	115%
Germany	149% ³

However, labour costs are only one factor in determining investment decisions and hourly wage rates are just one indicator of employment cost. Productivity is measured by the value generated by an hour's work. As noted above, a full analysis of all the cost, quality and delivery aspects of procurement is needed to determine the optimum manufacturing location. Analysis of available statistics indicates that UK automotive industry productivity is growing (up by 58% from 2000 to 2005 in terms of value added per person), and that UK manufactured automotive products are commanding a higher price in the market.

6. Analysis of international energy costs suggests that the UK is not necessarily disadvantaged by the level of electricity and gas prices faced by large industrial users like automotive companies, although there was understandable concern about the volatility of UK prices. We also note that the European Competition Commissioner seems determined to continue to put pressure on Member State Governments to remove such barriers to competition in the energy market as price caps for industrial consumers. This, and the recent signs of decreases in UK gas and electricity prices, may reduce or eliminate the cost disadvantage recently felt by companies with manufacturing operations in the UK. (Paragraph 38)

We note the Committee's comments on energy costs and understand the concerns of industry about recent higher prices and price volatility. The Government works to ensure the continuity and security of energy supply at affordable prices through competitive markets, whilst minimising environmental impacts and delivering social objectives. We have been encouraging the European Commission to implement energy market liberalisation across the EU, and warmly welcomed the robust actions in 2006, such as anti-trust action and infraction proceedings.

7. As our predecessors suggested, skills and training are critical issues "in an industry where processes are increasingly high-tech and innovation and adaptability

³ Source: <ftp://ftp.bls.gov/pub/special.requests/ForeignLabor/ind3361naics.txt>

are crucial and where persistent skills shortages could threaten the UK's continued success". The two and a half years since our predecessors' Report is, perhaps, too short a timeframe to expect much improvement in a longstanding problem like the skills shortages in the automotive industry. The Automotive Academy, opened in 2004, was eagerly anticipated as an innovative approach to the problem, and it seems that it has represented a new commitment from all parties—the individual companies, trade unions and Government—to addressing skills needs. In fact, the Government regards it as being such a success that it has decided to build on this model for a National Manufacturing Skills Academy. The Automotive Academy is being merged into the new body. It is not clear to us what, if any, implications this has for the future of training for the automotive industry. We would welcome an explanation from the Government of the reasons for this surprisingly early change to the structure of training for the industry, with its associated risk of a loss of focus on the needs of the automotive sector. (Paragraph 43)

Almost 3,000 people received training under the auspices of the Automotive Academy (AA), leading to over 6,000 improvement programmes in the workplace. The 2005 Skills White Paper, *Getting on in business, getting on at work*, identified the Automotive Academy as a good model for a National Skills Academy. Government took the view that it was important to expand this model sooner rather than later across other manufacturing sectors. Clearly it would not be sensible to have two Government-sponsored bodies competing and potentially duplicating activities. It was felt that integrating the Academy as part of the National Skills Academy for Manufacturing (NSAM) would enable the wider manufacturing base in the UK to benefit from the successes gained in establishing and running the Academy and delivering demand-led training materials—including capitalising on the experience of operating a central hub and regional spoke business model.

The automotive sector is one of the cornerstones of NSAM and automotive companies are playing a key role. In particular, Nissan is the lead company for the North East region and Ford is the lead for London. Toyota is also closely involved in the Academy. All sectors will gain from access to a wider range of resources and transfer of best practice from related sectors. Economies of scale should also mean that any funding is more focused on training rather than administration. Overall, our objective is that the merger of the AA into the NSAM should have no negative effect for training in the automotive sector.

8. We note that the whole issue of 'low carbon' transport is being addressed again in the context of the Government's Energy Review. We hope that this will lead to a consistent and long-term approach to research funding. We also seek the Government's views on GM's and Ford's suggestions about how to improve the R&D base. These are subjects to which we intend to return in a future inquiry. (Paragraph 46)

We fully agree that the development of low carbon transport should be seen as a priority both in terms of environmental improvements and business opportunities which is why we announced the Low Carbon Transport Innovation Strategy (LCTIS) in the Energy Review. In terms of funding, the Budget announced that the Technology Strategy Board, in partnership with Department for Transport (DfT) and the Engineering and Physical

Sciences Research Council (EPSRC), is planning to launch a Low Carbon Vehicle Innovation Platform. Further details will be contained in the Energy White Paper which will be published this month. The LCTIS will be published alongside the Energy White Paper. In addition, we have also announced that Professors Julia King and Sir Nicholas Stern will conduct a review on new vehicle and fuel technologies which could help decarbonise road transport, particularly cars over the next 25 years. The initial report of this work will be published at the time of the 2007 Pre-Budget Report.

GM mentioned the West Midlands in particular. Advantage West Midlands' (AWM) Premium Automotive R&D (PARD) Programme is aimed at enhancing the manufacturing and design capabilities of automotive supplier companies particularly in the Midlands. 50 R&D work streams, aimed at catalysing R&D and transferring new technologies to the premium automotive supply base, have been carried out since 2003 with a total cost of £61.7 million (£32.7m from AWM and £29m of industry match funding) and the involvement of over 150 companies in the supply chain. The programme is on target to achieve the government-defined economic outputs agreed with AWM (e.g. over 150 new products and processes; over 5000 jobs safeguarded) and has also achieved additional benefits.

With regard to Ford's suggestion of linking payments for R&D tax credits more closely with the PAYE/NIC payments, Government considered this issue in the 2005 R&D Tax Credits discussion paper exercise. Having considered the experience of other countries with similar systems (e.g. Netherlands), we concluded that a linkage with the PAYE/NICS system would add too much complexity to the scheme. The Government will keep policies under review based on evidence from across the economy.

9. We are delighted that the industry wishes to build on the highly-regarded research facilities in this country, and note that even companies which have been closing production facilities, such as Ford and GM, are using the UK as a research base for their worldwide operations. We note that the Ford Motor Company claims to account for 'some 80% of UK automotive R&D'—whether by staff numbers or value is not specified. While welcoming Ford's commitment to the UK, this does make the efforts of the rest of the sector appear less impressive. We recommend the Government to review whether the UK is really still at the forefront of innovative design and technology in the automotive sector, or whether research facilities are being used for work to support technological developments elsewhere in the world. Again, this is a subject to which we intend to return. (Paragraph 47)

The Government acknowledges Ford's major contribution to R&D in the UK automotive sector which goes back many years. The scale of their commitment to the UK is very welcome and is exactly the kind of investment that Government is determined to work with other companies to nurture.

But this is not the whole story. Nissan's decision to relocate its European design Headquarters from Germany to London enabled its latest UK model—the Qashqai—to be designed in Paddington, engineered in Cranfield and built in Sunderland. In addition, the UK's long-established independent design engineering sector works with Vehicle Manufacturers from around the globe and offers the full spectrum of services from concept design to limited-series vehicle production. This sector, which includes

companies like Lotus, MIRA, Prodrive, Ricardo and Zytec, is recognised internationally for its flexibility, responsiveness and track record of innovation. The UK's design engineering sector is regarded as a world leader in engine and powertrain design and a major contributor of know-how in promising niche-vehicle start-ups such as the Modec range of battery electric vehicles. These facts provide compelling evidence of the breadth of the UK's automotive development base.

But we cannot rest on our laurels. Under UKTI's 5-year strategy 'Prosperity in a Changing World' (launched in July 2006), the Government is working to encourage innovative and knowledge-driven business growth, not least by R&D intensive companies, in selected sectors including automotive. Under this, UKTI seeks to attract innovative, foreign-owned companies in the automotive sector to the UK, or those already with a UK presence, to undertake R&D at the cutting edge of technological innovation. Active promotion of the UK's world-class position in automotive R&D is at the forefront of this work. Such investment and growth—as well as the potential for collaborations with the science base and global manufacturers—increases the sector's diversity, including in R&D, and adds to its overall competitiveness.

DTI has commissioned a Sector Competitiveness Analysis on the 'Competitiveness and Productivity of the UK Independent Design Engineering Sector' serving the automotive and electronics industries. The report is nearing completion and is expected to be published on the DTI website in the near future.

10. There is a lingering suspicion that companies strongly connected by ownership, management headquarters or production capacity with a particular country will, unless countervailing arguments are overwhelming, choose to err in the direction of axing jobs overseas rather than at home. It is possible that the Japanese companies which have shown such strong commitment to the UK have been, at least in part, motivated by the fact that the UK has been their 'home base' within Europe. (Paragraph 48)

The presence of seven of the global top ten vehicle manufacturers in the UK demonstrates the sustained commitment and value accorded to the UK by overseas investors. These companies make hard commercial decisions on the basis of a range of factors including productivity, the skills and flexibility of the workforce etc and a committed, supportive Government. We have seen that a number of these companies have had to take tough decisions affecting employment in their home countries over recent years. For example, Nissan are looking to cut 1,500 jobs in Japan, and PSA are to cut up to 5,000 jobs in France, as the companies look to realign capacity with demand. And as noted above, decisions like the one on Ellesmere Port demonstrate the continuing relevance of the UK as a major automotive manufacturing location.

Ryton and Ellesmere Port

11. The job losses at Ryton and Ellesmere Port appear to have resulted from a combination of causes. The fundamental one, for volume car producers, is the excess production capacity in areas of the world (including Western Europe) where demand is stagnant or falling. This does not mean that the UK automotive industry is doomed; but it does indicate that individual plants which are old-fashioned and

inflexible, are simple assembly plants, are remote from the company's supply chain, produce only one main model, and have productivity or skills problems will be vulnerable. There may be large-scale job losses, such as those seen at Ryton and Ellesmere Port, in the UK automotive industry in future. It is therefore all the more important that lessons are learned from the experiences of dealing with the mass redundancies arising from the collapse of MG Rover. (Paragraph 52)

The Government believes that there are very significant differences between the loss of the third shift at Ellesmere Port and the closure of Ryton. As HMG made clear at the time, PSA's decision to close Ryton was very much to be regretted. It was, of course, ultimately a matter for the company and was taken for a range of reasons. But it should be noted that the CEO of Peugeot said at the time that "the decision is in no way a reflection of the quality of either the Ryton workforce or the UK as a place to do business". It is also notable that the further investment destined for Slovakia rather than Ryton will not now proceed.

In the case of GM Vauxhall's Ellesmere Port site, the loss of the third shift was necessary to adjust Astra production volumes as the current model aged and demand waned. Significantly, the loss of the third-shift was generally seen as positive within the context of the plant's long-term future—to improving productivity and enhancing the competitive position as Ellesmere Port competed for the 'New Astra'. Although one shift was removed at Ellesmere Port, production did not fall by a corresponding third, suggesting that the plant's efficiency increased; an important factor in the plant successfully securing a place as one of the production sites for the 'New Astra' model. That decision demonstrates, of course, that it is possible for UK plants to overcome disadvantages such as logistical costs when competing for investment, even against the stiffest of competition.

The Government's response to the Committee's comments on lessons from the MG Rover Task Force is given below.

Lessons from the MG Rover Task Force

12. We note the differences in estimates of the employment rate of former MG Rover workers. Some former employees never claimed benefit or used any of the Task Force services, 'disappearing' into the general population. Even amongst those who did take advantage of support, advice or training, there was no requirement for them to keep the Task Force, or subsequently Advantage West Midlands, informed of their situation. Leaving aside actual numbers, it seems reasonable to conclude that the majority of those made redundant have found new jobs, but many have had to take a cut in salary, and some are doing less skilled work than they did at Longbridge. However, some of those forced to choose entirely new careers have found greater job satisfaction, even though the pay is lower. (Paragraph 68)

13. The NAO's report made recommendations on a number of issues, including the need for those providing training and employment advice to take into account the experience and requirements of all staff employed (managerial, unskilled, shopfloor, technical, office and support) and not to concentrate on one section (in the case of MG Rover, on manufacturing and engineering staff) rather than the others; and the

need to ensure that the support and information provided on training and employment opportunities is “made available at a time and is delivered in a manner which is most beneficial to the recipients”. We endorse these recommendations. (Paragraph 78)

14. On balance, the Task Force was a success, though, as with most disaster management, a number of areas—in particular, training provision—could have been improved if more time had been available. Useful lessons have been learned in how to address large-scale redundancies in future, and we detected that the relevant public bodies and PSA and GM appeared to have absorbed some of them in their longer-planned approach to the job losses at Ryton and Ellesmere Port. We look forward to hearing from the Government how it intends to address the specific weaknesses raised by our witnesses, especially those resulting from conflicts between training and benefit policies, such as the 16 hour rule. (Paragraph 84)

It is important to remember that redundancies in the UK are at a historically low level and make up a small part of all job separations—the vast majority being those who leave work voluntarily. Most redundancies happen in small numbers and events such as those at MG Rover remain the exception. Nevertheless, valuable lessons have been learnt. DTI has been working closely with the Department of Work and Pensions on a framework for redundancies to set out best practice in handling major redundancy events, drawing on the experience gained from MG Rover and other examples of large-scale redundancies.

The Government wishes to acknowledge the important contribution of the MG Rover Task Force, Advantage West Midlands, Job Centre Plus, Birmingham City Council and other local agencies in responding to the events at Longbridge. A number of these organisations are engaged in continuing activities to help individuals and the communities affected.

The MG Rover Task Force report recommended a review of the 28-day rule where a large-scale redundancy has put pressure on training places and a redundant person might need to look for temporary work lasting more than 28 days whilst waiting for a course to start. In the case of MG Rover, this rule was waived. The redundancy framework will be considering issues such as the 28 day rule.

There is a long-standing requirement for those claiming unemployment-related benefit to be available for and actively seek work—an issue commonly referred to as the “16-hour rule”. The MG Rover Task Force report recommended a targeted approach to allow individuals to undertake vocational training of more than 16 hours a week by accessing a training allowance from Jobcentre Plus. Opportunities already exist for claimants of Jobseekers Allowance (JSA) to access full-time provision funded by a training allowance, though this support is concentrated on the most disadvantaged, including those with basic skills needs. Access to allowance-funded training provision will be considered within the work to progress the Leitch skills agenda.

Advantage West Midlands continues to monitor employment statistics. The latest figures available indicate that 92% of former employees of MG Rover have now left benefit (5,846 out of 6,346), with 84% known to be in work. An evaluation of the MG

Rover Phase 1 activity has been initiated. Ecotec Consultants have been engaged to look at the economic impact of the activity undertaken in Phase 1 and the report will be publicly available in July 2007.