PREM19

44

ENERGY

(future of BNOC &

BP shares)

(Part 1)

SR
830

PREM 19/44

MT

PART 1.

SECRET

Confidential Filing

The future of BNOC
Proposed sale of BP ~~shares~~ assets

ENERGY

Part 1.

JULY 1979

Referred to	Date	Referred to	Date	Referred to	Date	Referred to	Date
~~18.7.79~~							
~~24.7.79~~							
~~26.7.79~~							
3.8.79							
~~4.8.79~~							
~~28.8.79~~							
~~[illegible]~~							

PREM 19/444

10 DOWNING STREET

First paper on file 2/7/79:

Earlier papers on

BNOC; BP Assets on

Econ Pol: June 1979

Privatised public Sector

PART 2 begins:-

S/S Energy to PM 13.9.79

PART 1 ends:-

IL to PM 12.9.79

TO BE RETAINED AS TOP ENCLOSURE

Cabinet / Cabinet Committee Documents

Reference	Date
E(DL)(79)6	2.7.79
E(DL)(79)7	3.7.79
E(79)20	13.7.79
E(79)22	13.7.79
E(79)21	13.7.79
Limited Circulation Annex to E(79) 5th Meeting, Minute 6	17.7.79
Limited Circulation Annex to E(DL)(79) 4th Meeting, Minute 1	19.7.79
E(79) 6th Meeting, Minute 1	24.7.79
E(79)31	7.9.79
E(79)36	7.9.79
Limited Circulation Annex to E(79) 7th Meeting, Minute 4	11.9.79

The documents listed above, which were enclosed on this file, have been removed and destroyed. Such documents are the responsibility of the Cabinet Office. When released they are available in the appropriate **CAB** (CABINET OFFICE) CLASSES

Signed C M Wayland Date 16 September 2009

PREM Records Team

PRIME MINISTER

8.9.79

This letter from John Hannam, MP, is written on behalf of "Energy Backbenchers". He urges that we do not sell off BNOC assets. He also argues that we should split BNOC into a trading company, and an exploration and production company with maximum private sector investment. This is, of course, precisely the route we have now decided on.

You will of course wish to reply after Mr. Howell's statement. He is clearing a draft with the Chancellor, and hopes to submit it to you tomorrow. He will submit, at the same time, a draft letter for you to send to Mr. Callaghan, and I will arrange for a draft for you to send to Mr. ~~Howell~~ Hannam.

Thank you

R.

12 September 1979

VB

12 September 1979

I attach a copy of a letter which the Prime Minister has received from Mr. John Hannam, MP, about BNOC. I would be grateful if you could provide a draft reply which the Prime Minister could send as soon as possible after Mr. Howell's statement.

You promised on the telephone this morning to let us have a draft also for the Prime Minister to send to Mr. Callaghan on this same timescale.

TPL

W.J. Burroughs, Esq.,
Department of Energy.

vb

12 September 1979

I am writing to acknowledge your letter of 8 September to the Prime Minister about the future of BNOC, which I have of course placed before her. A reply will be sent to you as soon as possible.

TPL

John Hannam, Esq., M.P.

Energy

10 DOWNING STREET

11th September, 1979

PRIME MINISTER

The present value of the Statjford Field is roughly divided as follows :

Oil	£230m +	£250M.
Gas	< £20m	

These figures have been checked with the Department of Energy.

David Wolfson

cc Mr Wolfson

Qa 04255 CONFIDENTIAL

To: MR LANKESTER

From: SIR KENNETH BERRILL

Forward Sales of North Sea Oil

The figures you wanted are:-

(a) £700m. is 175,000 bpd (at $25 a barrel)

(b) In 1980 BNOC expect to handle over 800,000 bpd on a rising trend as follows:

	Q 2	Q 4	
Government Royalty oil	200	250	90% refined in UK
BNOC "own" oil	600	650	60% " " "
	800	900	

(c) BNOC "own" oil is made up of -

	Q 2	Q 4	
Equity oil	90	120	← £350m
Participation oil	450	475	←
Purchases (net)	60	55	
	600	650	

(d) So 175,000 bpd is about 1/5 of total BNOC handling and rather under 1/3 of BNOC "own" oil. It is a higher proportion of BNOC's own oil sold for refining in the UK but there is still very adequate room for manoeuvre and BNOC would not have to agree forward payments with every major "user". The length of BNOC forward commitments to supply could vary from 1 to 5 years depending entirely on HMG's choice of rising income profile for 1981-4.

I am sending a copy of this minute to Sir John Hunt.

K.B.

KENNETH BERRILL

11 September 1979

CONFIDENTIAL

10.9.79

Energy

1715

/7/

HOWELL REBELS OVER OIL SALE

ENERGY SECRETARY DAVID HOWELL IS BACKING THE STATE-OWNED OIL COMPANY'S CAMPAIGN AGAINST GOVERNMENT PROPOSALS TO SELL OFF ITS NORTH SEA ASSETS, INFORMED SOURCES DISCLOSED TODAY.

HE APPEARS TO SHARE OPPOSITION LEADER JAMES CALLAGHAN'S CONCERN, VOICED IN A LETTER TO PRIME MINISTER MARGARET THATCHER, THAT SUCH A MOVE WOULD BE ''SELLING THE SEED CORN OF THE FUTURE''.

MR HOWELL IS TRYING TO CONVINCE MRS THATCHER AND THE TREASURY THAT DISMEMBERMENT OF THE BRITISH NATIONAL OIL CORPORATIO WILL NOT BE IN THE NATIONAL INSTEREST.

IN THE 1980'S, HE BELIEVES, IT WILL BE A SOURCE OF ''TREMENDOUS PROFITS'' FOR BRITAIN.

1726

RACING

5.00 WINDSOR (24 RAN)

1 HAY REEF 9-4 FAV

2 SECATEURS 10-1

3 TANSOR 20-1

1728

I

1 ZIMBABWE

RHODESIA TALKS START ON TIME

ALL THE DELEGATIONS FOR THE ZIMBABWE RHODESIA CONFERENCE ARRIVED AT LANCASTER HOUSE IN LONDON TODAY AND THE CONFERENCE BEGAN ON TIME AFTER SOME BEHIND-THE-SCENES DIPLOMACY OVER WHO SITS WHERE.

FOREIGN SECRETARY LORD CARRINGTON, CHAIRMAN, GAVE HIS OPENING ADDRESS WHICH OUTLINED BRITISH THINKING ON A NEW

Mr Whitmore

Prime Minister
I think the idea of forward sales should be vigorously pursued. This will take care of the Chancellor's PSBR problems in 1979/80. For 1980/81, I think we should now consider 'privatisation' of BNOC as an alternative to selling off assets: politically easier and it can bring in as much money.

Qa 04254 CONFIDENTIAL

To: MR LANKESTER

From: SIR KENNETH BERRILL

Disposal of Energy Assets

1. When this item is discussed tomorrow by 'E' Committee I would urge the Prime Minister to pay particular attention to the forward sale of the North Sea oil aspects of this question. This is covered in the Secretary of State for Energy's paper but is not given quite the full attention it deserves - in part because the proposal surfaced only recently and in part because when Mr Howell wrote his paper it was not completely clear that such forward sales of oil would count against the PSBR, but that has now been resolved.

10/9

2. We start from the need to obtain £1 billion to help reduce the PSBR in the present financial year, of which £700 m. must come from some combination of BP shares and the North Sea. The whole of £700 m. could be obtained by selling forward a large part (but by no means the whole) of BNOC's 1980 oil from the North Sea. The terms of the forward sale would be that the Government (through BNOC) would be paid for this oil at the beginning of the year rather than for delivery during the year. In exchange for this payment in advance the oil companies concerned would be guaranteed a supply of North Sea oil for their UK refining operations to the value of £700 m. for periods of between 3 and 5 years. At the end of these periods the payment would revert to the normal timing.

3. This is in fact early payment in exchange for security of supplies to the company's UK refineries. Clearly, when the period of each undertaking expires the Government will have to wait awhile before it begins to get paid again. But this problem can be spread over 2 or 3 years by

CONFIDENTIAL

varying the timing of the contracts and the problem will be eased by increases in the volume of North Sea oil and by any increase in the price of oil per barrel.

4. From the Government's point of view the advantages of such forward sales are two-fold. Firstly it is the only way in which, in practice, the Chancellor can get £700 m. by next March. The sale of BP shares will raise money within this timescale but the sale of any North Sea assets will take appreciably longer.

5. As has already become apparent, BNOC will be a most unwilling seller and will argue for a high price; the value of the assets will vary from buyer to buyer according to the buyer's corporation tax postion; BP are aware that the Government wants to sell only the British company; BNOC wants to sell gas, whereas BP want to buy oil - it all has the makings of a long drawn out and unpleasant operation.

6. But apart from forward sales having the advantage of getting the money into the Chancellor's hands quickly they do provide the alternative of being not just a temporary substitute for the sale of assets, but a complete substitute. Given Ministers' unhappiness at being forced to sell BP shares and the practical difficulties of selling BNOC assets the advantages are great.

7. It is important to realise that since Ministers first discussed the sale of BP shares and the sale of North Sea assets to BP, the circumstances of that company have greatly changed. A year ago BP was in the comfortable position of having 180 million tons of crude oil worldwide and needing only a 100 million tons for their own refineries. The events in Iran, Kuwait and most recently Nigeria have changed this dramatically. BP now have appreciably less than the 100 million tons they need and may be forced to pay high prices in the spot market in the coming year to meet their needs.

8. The market is just beginning to appreciate this position which is likely to affect the BP's ability to purchase North Sea assets on a large scale without a rights issue. Besides having implications for the sale of BP shares and the sale of North Sea assets to BP, this new position makes it very important to try to make any North Sea oil which is surplus to the UK's requirements available to BP for overseas refining so as to help a major British company with its difficulties. This last is not an issue immediately before Ministers but it, together with the reorganisation of BNOC, will be important questions in the immediate future.

9. I am sending a copy of this minute to Sir John Hunt.

KB

KENNETH BERRILL

10 September 1979

Prime Minister

The Foreign Secretary and Lord Privy Seal would, of course, be glad to attend. There is an FCO interest. Can Mr Ridley come instead?

Ref: A0197

CONFIDENTIAL

PRIME MINISTER

BNOC Disposals (E(79) 36) Yes MT 10/9

Although I have bracketed this on the Agenda with the Chancellor's paper (E(79) 31), you will probably find it convenient to take the BNOC paper first. If you can secure agreement on the Energy proposal, you can then score £400 million safely before moving on to discuss the Chancellor's proposals for raising the rest of the money.

BACKGROUND

1. Earlier discussion on this subject stretched over several meetings of E and E(DL) and resulted in an instruction to Mr. Howell to go away and find £400 million in the current financial year, from disposal of assets rather than by any other financial device. He has since had extensive talks with BNOC and BGC, and with BP (and some of this has leaked into the Press). You discussed this with him last week, with results reported in your Private Secretary's letter of 5th September; you might also look again at the note from the Chancellor's Private Secretary of 7th September. The net position is that the Secretary of State can find his £400 million, but not necessarily in the current year; that (subject to detailed checking) the Chancellor is prepared to accept this, provided that the shortfall could be made good temporarily in the present year; but that the sale of BNOC assets will be quite difficult and has some nasty side effects.

HANDLING

2. I suggest you ask the Secretary of State for Energy to introduce his paper, and then, before too many general comments from other Ministers, try to structure the discussion around these questions:-

(a) Can the £400 million be found by sales of Viking and Statfjord? -Oil.

The BGC option has dropped (though perhaps Mr. Howell is unduly conscious of Sir Denis Rooke's susceptibilities). So he proposes to raise the whole of the money from sale of Viking, -Gas. and associated developments, and of Statfjord. (N.B. this is the BNOC interest on the British side of the line, but because the field is unitized, this

requires the agreement of all the partners, among whom Phillips is the predominant one). There are four main problems:-

(i) BNOC's declared opposition. There is no doubt that the Corporation will lose staff, and quite possibly some Board members if this sale goes through. Since it is now agreed Government policy to keep BNOC in being, on a reduced scale, this is a factor: but Mr. Howell is prepared to accept the risks.

(ii) The chances of getting a good price. BNOC themselves regard these as sub-commercial deals, and will say so. They will require a direction. This is a political issue. There will be a major Parliamentary row (see Mr. Callaghan's remarks at the week-end): but this may be tolerable.

(iii) Timing. It is pretty clear that a transaction of this scale could not be completed in the current year notably because of the uncertainties about the gas interests associated with Viking, and about Statfjord. So the acceptability of the package turns on the acceptability of the bridging operation - see below.

(iv) The role of BP. The Committee was strongly inclined, last time, to make sure that these assets ended up with BP. It will not necessarily follow that the Government can control the oil as effectively: BP exports more oil than BNOC and will continue to do so. But the bulk of the planned disposals are of gas, which has perforce to land in this country. More serious is the net effect on the PSBR: any purchaser would offset the purchase cost against tax liabilities, but because BP's profitibility is currently so high, the tax loss would be particularly great. You might probe the Chancellor's views on this. (It may be that the interest saved by having £400 million in cash will largely offset the loss of revenue.)

The device proposed for ensuring that BP pays a fair price is also questionable, but should be all right. You might see whether the Lord Privy Seal (Mr. Ridley) (in the Foreign Secretary's absence) is content.

(b) Is there a viable alternative i.e. by selling oil forward?

Mr. Howell touches on this in paragraph 10, but does not specifically recommend it in paragraph 13. However, BNOC are pressing hard in private for a series of forward oil sales as a permanent alternative to the disposal of assets. They argue that it will have the same effect on the PSBR, without involving loss of control or of future profitibility. You might see whether Mr. Howell wishes to pursue this point seriously. If so you will need to check with the Lord Privy Seal about the possible impact on OPEC practice - see the Chancellor's Private Secretary's letter of 7th September.

(c) Is the forward sales device useable as a short term bridging operation?

Subject to the same OPEC point the forward oil sale device might be considered as a temporary bridging operation even if it is not acceptable as a permanent solution. The Chancellor's provisional view (which needs to be confirmed after work by officials) is that if BNOC sells its own oil forward, the proceeds will help to reduce the PSBR; whereas if the Government sells its royalty oil, this will not. Provisional CSO advice confirms this. The real point however is that if permanent asset sales cannot be achieved this financial year and if the forward oil sales device is not acceptable, then either the Chancellor has to abandon the £1,000 million target for this year (with the consequences pointed out in his own paper) or something else has to be sold, probably more BP shares.

CONCLUSIONS

3. The most likely outcome of the discussion seems to be that the £400 million worth of assets should be sold, in the way proposed by the Secretary of State for Energy (paragraph 13(i) and (ii)); and that the PSBR target in 1979-80 should be temporarily bridged in the method proposed at paragraph 13(iii).

4. In any case, the Committee should take note that the Secretary of State will be making further proposals about a new capital structure for BNOC.

(John Hunt)

10th September 1979

10 SEP 1979

26

Ref: A0196

SECRET

PRIME MINISTER

Disposals of Public Assets in 1979-80
(E(79) 31)

BACKGROUND

I have already suggested that you should take this paper after the paper from the Secretary of State for Energy.

2. As with that paper, the background is familiar to you. The essential question is whether to sell BP shares this year, having made the maximum possible disposal of other assets.

3. Following the Committee's last discussion, the Treasury has once again trawled all round Whitehall, with the results reported in the Chancellor's paper. £400 million of this will have been settled under the previous item of the Agenda. There are some detailed points to check on the other sales. But the main discussion is about BP.

HANDLING

4. You should invite the Chancellor of the Exchequer to introduce his paper. You might then take the 'score-card' first and briefly. You could go quickly through the six items listed in paragraph 2. The only difficult one looks like being the sale of The Radio Chemical Centre (TRC), where there may be difficulties about selling all £30 million of the shares. The total might thus have to be written down by £15 million to allow for sale of only half. The other sales seem fairly secure. You might confirm that the Ministers concerned are content.

5. The discussion then focus on BP. The Chancellor's paper sets out the issues quite clearly. You have yourself always been reluctant to agree to this sale, particularly in the near future. You may wish to discuss briefly with the Chancellor before the meeting whether to sustain this line. If you do, then there seems no way of avoiding a shortfall on the £1,000 million target. If you are now prepared to see a limited sale go forward, then the issues listed in paragraph 10 should be considered one by one.

(i) Timing. Left to you to settle with the Chancellor: no problems.

(ii) Sales Abroad. The Committee should distinguish between the place of sale (London and/or New York) and the purchaser: nothing can stop foreign investors buying BP shares, wherever the marketing takes place. It is not proposed to offer any of the shares privately to overseas investors, despite nibbles.

(iii) Preferences. There should be general support for these proposals.

(iv) The form of the issue. There is no reason for the Committee to object to the largely-technical points here. You may want to discourage too much detailed discussion: these are really matters for the Chancellor and the Bank.

CONCLUSIONS

6. The conclusions might be:-

(i) to note the progress made towards the £1,000 million target (including the £400 million from BNOC, if that has earlier been approved), /and with any modifications made as a result of discussion, specially on TRC/;

(ii) to agree that approximately 7 per cent of BP stock should be sold;

(iii) to endorse the practical details set out in paragraph 10 of E(79) 31.

(John Hunt)

10th September 1979

John Hannam, M.P.

Secretary
01- 219 4189

HOUSE OF COMMONS
LONDON SW1A 0AA

Messages
01- 219 4343

8th September, 1979.

F12/9

Dear Prime Minister,

In view of the public controversy over the proposed Government action to deal with the British National Oil Corporation, I felt I must write to express the hope of 'Energy Backbenchers' that we do not embark upon a short-term sell-off of some BNOC assets, but rather that we keep the upstread section in tact. This will enable us to float a substantial shareholding of BNOC in the near future followed by further stock sales in future years building up to a "B. P. type' formula with ever-increasing private sector investment.

The need to maintain an effective British stake in the North Sea plus security of oil supplies can best be served by a separation of BNOC's activities into companies. One a trading company handling the participation oil, the other an exploration and production company run on B. P. lines with maximum private sector investment and management.

The sale of choice oil holdings of BNOC at this stage might bring in some much-needed cash on a 'once and for all basis but it would it not benefit our longer-term objectives of security ofsupply and free enterprise British Oil Industry development.

/ over . . . . .

I hope you do not mind me expressing these views which reflect the thoughts of those of us who have been engaged in Energy Committee work for a number of years.

Good luck in all your endeavours.

Yours ever,

John

The Rt Hon. Margaret Thatcher, M.P.
10, Downing Street,
London, S.W.1.

From: The Rt. Hon. James Callaghan, M.P.

HOUSE OF COMMONS
LONDON SW1A 0AA

7 September 1979

Dear Prime Minister,

I am writing to ask you for information about the reports that you intend to instruct the British National Oil Corporation to sell part of the resources of oil and gas in the North Sea owned by them on behalf of the nation. If these reports are true, I must warn you that such a decision would become a major issue between us going far beyond the normal divisions between Government and Opposition. In our view such a decision by your Government would be totally against the national interest, which lies in owning and exploiting the one secure source of oil this country possesses.

At present we have this through the ownership interest of the BNOC, which ensures that the oil and gas come directly under the control of the British Government in a way that can apply to no other source of oil and puts this country in a stronger position economically than any other major industrial nation. To dispose, or lose control, of part of our national resources would be to sell the seed corn of the future.

My understanding is that the assets whose disposal are now under discussion, will be producing substantial quantities of oil as well as revenue for this country to the end of the century and beyond.

/ As regards

As regards the revenue that the Government would secure, the truth is that you would be requiring the BNOC to make a forced sale and in financial terms they would run the gravest risk of not obtaining the full value, especially as I assume that there could be no question of allowing these assets to be sold to companies controlled overseas.

In recent years the Labour Government successfully built up a method of controlling North Sea oil which is compatible with our international obligations to the EEC and under GATT, and the Government should do nothing by its actions to weaken this position.

As you know, many overseas interests would like to call our present position in question and we have recently seen how British oil companies have had their vital supplies affected by the decisions of foreign governments. This is no time for us to weaken in any way the strength of our supply position.

I remind you that the BNOC was established as the direct outcome of a Parliamentary Inquiry and a recommendation by Members of all Parties in 1973 when there was, at that time, national concern about the shortcomings of the then Conservative Government's oil policy as regards ownership, revenue and national control. To sell BNOC assets is totally against the national interest and I shall be grateful for your assurance that the present discussions will not lead to the disposal of any North Sea oil field or part of it at present owned by the BNOC and that you will ensure that the fullest control and ownership of these natural resources and national assets will be protected by your Government.

/ In view of

In view of the importance of this matter and the fact that I have been informed that decisions are likely to be taken during the coming week, I shall be releasing this letter to the press.

Yours sincerely,

pp Jim Callaghan
D.

The Right Honourable Margaret Thatcher, M.P.

cc Prime Minister 2

E Energy

PRIME MINISTER

As I asked Joyce Humphris to tell you, Mr. Callaghan has now written you the attached letter about reports of the disposal of BNOC assets. He says that he is releasing it to the press in view of the wide public interest and the likelihood of early decisions.

I have sent copies to Mr. Howell's office, and to the other members of E Committee, and have asked Mr. Howell to provide a draft reply for you to send, but not to submit it until after the discussion at E on Tuesday.

7 September 1979

CONFIDENTIAL

To go with the papers for it on 11 Sept.

PRIME MINISTER
The Chancellor's comments on BNOC disposals. Mr Callaghan's letter to you on this is also in the box.

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

7 September, 1979

7/IX

Dear Ian,

DISPOSALS AND THE PUBLIC SECTOR BORROWING REQUIREMENT 1979-80

The Chancellor of the Exchequer has seen your letter of 5th September about the Prime Minister's conversation with the Secretary of State for Energy on the asset disposal programme. You reported the Prime Minister's view that provided that the BNOC and BGC sales programme was underway by March 1980, and subject to the Chancellor's views, she thought that it might be acceptable for market confidence and the Government's monetary objectives, if the completion of the £400m programme slipped two or three months into 1980-81.

The Chancellor has since discussed this with the Secretary of State for Energy and he well recognises the Secretary of State's difficulties in these matters. Equally, however, to permit the degree of flexibility suggested would, of course, mean that the sale proceeds were not received until 1980-81 with the inevitable result that the Public Sector Borrowing Requirement for 1979-80 would be higher by £400m.

The Chancellor must regard any failure to meet the Government's Budget commitments on the PSBR as a very serious matter indeed, going right to the heart of the Government's monetary and fiscal stance which is central to its strategy. Both the PSBR and the money supply are currently running high and there is no scope for relaxation if the targets are to be met. In particular, there is nothing in the present situation which provides any grounds for hoping that the Government could meet its PSBR objectives without the full £1bn contribution from asset sales. The Chancellor also believes that credibility in the Government's determination to carry through its monetary and fiscal programme would be put in serious jeopardy if the PSBR target

/announced

T. Lankester, Esq.,

announced in the Budget was missed because of the Government's own failure to carry through decisions already announced. The public conclusion would inevitably be that having failed to meet a PSBR target once, the Government could well do so again. Such a conclusion could seriously dissipate the hard won confidence built up during the last few months.

But as I said earlier, the Chancellor does indeed recognise the Secretary of State's difficulties and therefore he has asked his officials to use their utmost ingenuity to see whether a way can be found of reconciling the conflicting interests of meeting this year's PSBR target and delaying a £400m sale of BNOC/BGC assets until early in 1980-81. Officials have already met with BNOC and are considering in particular a possibility involving advance payments for oil contracts. It is by no means clear that this could be presented as a credible reduction to the PSBR (as distinct from a financing transaction). Even if it could, the arrangement might well create problems if the OPEC countries sought to adopt similar arrangements for their contracts. The Chancellor will report his conclusions to E Committee on Tuesday.

I am sending a copy of this letter to Bill Burroughs (Department of Energy), to George Walden (FCO) in view of the possible consequences for relationships with OPEC of any BNOC deal of the sort described in paragraph 4 above and to Martin Vile (Cabinet Office).

Yours ever,

Tony Battishill

(A.M.W. BATTISHILL)

7 SEP 1979

tmw

c.c. HMT
HO
FCO
DI
Ld.Pres.
DM
MAFF
DTrade
Ch.Sec.
Cab.Off.

B/F 14.9.79.

7 September 1979

I enclose a copy of a ~~letter~~ 7.9 to the Prime Minister from the Leader of the Opposition about reports that BNOC is to be instructed to sell some of its assets. Mr. Callaghan makes it clear that he is releasing his letter to the press.

I expect that the Prime Minister will want to reply personally to Mr. Callaghan after the discussion at E Committee next Tuesday. Perhaps you could put in hand the preparation of a draft reply, although you will not wish to forward this until the decisions of that meeting are known.

I am sending copies of this letter to the Private Secretaries to the other members of E Committee and to Martin Vile (Cabinet Office).

M.A. PATTISON

W.J. Burroughs, Esq.,
Department of Energy.

tmw

tmw

7 September 1979

In the Prime Minister's absence in Scotland today, I am writing to acknowledge your letter to her of 7 September, about reports that the British National Oil Corporation may be instructed to sell some of its assets.

I will ensure that the Prime Minister sees your letter today, and I know that she will want to reply to you as soon as possible.

CAW

The Right Honourable James Callaghan, M.P.

PRIME MINISTER 2.

Tim has probably given you advance warning of this

MAP 6/IX

PRIME MINISTER

One of the decisions on the future of BNOC which we reached in E Committee on 24 July was that BNOC should be asked to reduce its stakes in 1st to 5th round offshore licences. We reached this view because - as I announced in my subsequent statement to the House - it was clear that the Corporation had acquired too many licence obligations, and that its exploration commitments had become over-extended.

In pursuit of the remit this placed upon it, the Corporation has now identified a first batch of 30 exploration blocks (out of its total 1st - 5th round holdings of 108 blocks) in which it would be prepared, voluntarily, to relinquish its interests, and you and colleagues should be aware that it plans to invite bids for the blocks by means of advertisements in the national dailies either at the end of this week or next week. The majority of these are from the fifth round of licensing where the financial burden involved is most onerous and the exploration potential appears least rewarding: for this reason it is unlikely that farm-out of these interests would raise any substantial cash premium from buyers, but it would reduce BNOC's financial and management commitment and allow the Corporation to concentrate on work of higher priority.

I am copying this letter to members of E and E(DL) and to Sir John Hunt.

DH

D A R HOWELL

6.9.79

-6 SEP 1979

CONFIDENTIAL

FILE

Energy
cc HMT
cc CO
cc FCO

10 DOWNING STREET

From the Private Secretary

5 September 1979

Dear Bill,

The Prime Minister had a meeting with your Secretary of State yesterday afternoon to discuss various matters relating to BNOC.

In the course of this discussion, Mr. Howell referred to the remit which he had been given at E Committee on 24 July - namely, that he should arrange for sales of assets by BNOC and BGC to yield a net £400 million in 1979/80. He said that it would be very difficult to achieve sales on this scale by the close of this financial year. As he had repeatedly explained, this was going to be an extremely complex operation; and as long as BNOC's top management continued, their opposition to the sales would make them all the more difficult to achieve. Moreover, if the sale of assets was rushed, there was a real risk that it would have to take place at knock-down prices. Mr. Howell went on to say that he continued to have grave doubts about the political wisdom of selling off BNOC's assets, even though he fully accepted that the revenue somehow had to be found to meet the Chancellor's PSBR target.

The Prime Minister said that she was not prepared to reopen the decisions which Ministers had already taken on asset disposals. As regards timing, however, she recognised that there might be problems in achieving the full £400 million of BNOC and BGC sales by the end of March 1980. Provided that the sales programme was under way by then, and subject to the Chancellor's views, she thought that it might be acceptable from the point of view of market confidence and the Government's monetary objectives, if the completion of the £400 million programme slipped two or three months into 1980/81.

I am sending copies of this letter to Tony Battishill (HM Treasury) and Martin Vile (Cabinet Office).

Yours ever.

Tim Lankester.

W. Burroughs, Esq.,
Department of Energy.

APPOINTMENTS IN CONFIDENCE

NOTE FOR THE RECORD

c.c. David Wolfson
Clive Whitmore
Master Set
Appointments

The Secretary of State for Energy called on the Prime Minister at 1730 hours on Tuesday, 4 September, to discuss the Chairmanship of BNOC and related matters. They had before them Mr. Howell's letter of 30 August to David Wolfson. Mr. Howell said that the choice of a new Chairman for BNOC was inseparable from the type of organisation which the Government intended BNOC to be. Before discussing possible candidates, he wanted the Prime Minister to know that it would be very difficult to achieve the net £400 million sale of assets which E Committee had asked him to arrange before the end of 1979/80. Moreover, he had grave doubts about the political wisdom of pursuing this course. The Prime Minister said that she was not prepared to reopen the decisions taken by E Committee on asset disposals, but she thought there might be some scope for allowing the £400 million sales programme to slip two or three months into 1980/81. (This part of the discussion is further summarised in my letter of today's date to Mr. Burroughs.)

They then discussed various candidates for the succession to Lord Kearton. The Prime Minister said that it was essential to appoint someone with oil experience; but he would also need to be capable of managing the rationalisation and reorganisation of BNOC. Mr. Howell said that of the names he had suggested in his letter of 30 August, Mr. Ashley Rayburn of Rolls Royce was his first preference. He intended to see him the following day. If Mr. Rayburn were not available for the job, then he would try Sir Francis Tombs and Mr. Michael Pocock - the latter would be quite excellent <u>if</u> he were willing to serve after his retirement from Shell next year. The Prime Minister said that she agreed that Mr. Howell should proceed on this basis; of the other names he mentioned in his letter, she was unimpressed by Sir Ronald McIntosh as a possible candidate.

/Mr. Howell

Mr. Howell explained further his ideas for reorganising BNOC. He had in mind an oil trading organisation, and an oil company, with the BNOC main board presiding over both wings. The oil company would have a 49 per cent private shareholding. If this approach were pursued, it would be essential to recruit a strong man for the chairmanship of the oil company. But the first priority was to find a new Chairman for the main company, one of whose tasks would be to find suitable personnel for the two subsidiaries.

Finally, there was some discussion of possible candidates for a strengthened BNOC board. Mr. Howell and the Prime Minister agreed that the following would make good candidates: Mr. Phillip Shelbourne, Mr. Matt Linning, Mr. Ronald Grierson and Mr. Alcon Copisarow. Mr. Howell said that he would consider these and other possibilities further. The Prime Minister said that she was not keen on appointing Sir John Greenborough, nor did she think that Lord Rothschild would make a particularly good candidate; Mr. Howell, however, said that he would like to keep open the option of appointing Lord Rothschild.

TL

5 September 1979

CONFIDENTIAL

8/F 3.9.79.

cc Mr Wolfson

10 DOWNING STREET

From the Private Secretary

SIR KENNETH BERRILL

BNOC

The Secretary of State for Energy will be calling on the Prime Minister tomorrow to discuss the Chairmanship of BNOC and related matters. I understand that Mr. Howell will be putting forward certain suggestions for the future organisation of the Corporation: in particular, he proposes that BNOC be split into two bodies - an oil trading organisation and an oil company (in which the Government would only have a majority share). The BNOC Chairman and main board would preside over both bodies, with the Deputy Chairman on the main board being responsible for the North Sea company in which BNOC would have a 51% shareholding. The remainder of the shares would be split amongst as wide a range of the public as possible; one purpose of this would be to make renationalisation difficult and allow genuine public participation in the North Sea.

I would be grateful for briefing on these organisational aspects - which Mr. Howell rightly recognises need to be settled in broad terms before decisions are taken on the Chairmanship.

I am sending a copy of this minute to Sir John Hunt.

J. P. LANKESTER

3 September 1979

CONFIDENTIAL

Energy

CONFIDENTIAL

Qa 4245

To: MR LANKESTER

From: SIR KENNETH BERRILL

Prime Minister

I commissioned this note on Mr Howell's organisational proposals – I have not told the CPRS about the people he has in mind for chairman.

PL

3/9

BNOC

1. I have just received your minute telling me that the Prime Minister will be seeing the Secretary of State for Energy tomorrow to discuss the future organisation and chairmanship of BNOC and you asked if I would give you a note on the proposed organisational changes.

2. The CPRS has not been a party to these considerations and I have not thought it proper to contact anyone in BNOC this afternoon. The following comments are therefore my immediate reaction to these proposals and should be considered in that light.

i. The organisation of BNOC and the scale of BNOC's likely future operations clearly have an important bearing on the future chairmanship. Too large a sale of BNOC assets would affect both the likely efficiency of the reorganised company and the ability to attract a first class chairman.

As for reorganisation, the proposal to split BNOC into two parts (a trading company and a production company) fits well with the desire to sell 49% of the production assets remaining to BNOC widely to the British public.

ii. The financial relations between the two companies are obviously important. Shareholders in the production company will expect an "arm's length" relationship with the trading company so that they get a full market price for their product.

CONFIDENTIAL

iii. The profit and losses of the trading company would need to be kept separate. But would any profits of the trading company be available to be borrowed by BNOC or would they revert to the Treasury. (At present BNOC can use trading profits for production purposes which reduces BNOC's reliance on the Government or the outside market).

iv. Although the trading and production companies need to be kept at arm's length in financial terms there is much to be said for their keeping in close contact for other purposes. The trading company will be selling both production oil and (in much greater volume) participation oil. Detailed knowledge of the physical characteristics of different parcels of oil can be of value to the trader who is engaged in selling them. If the production side of the company could continue to help the trading side in this area the advantages which an integrated company have in this respect need not be lost.

Conclusion

Provided BNOC's total operations remain on a scale adequate to attract and retain first class staff there seems little to object to (and advantage in terms of selling of shares) in splitting BNOC into two companies. But the exact relationship of the two companies in both financial terms and in terms of exchange of information needs to be worked out in such a way as to try to retain the main advantages of an ingegrated company.

I am sending a copy of this note to Sir John Hunt.

KB

3 September 1979

CONFIDENTIAL

PECS

6/233/01

HM Treasury
Parliament Street London SW1P 3AG
Direct Line 01-233 5806
Switchboard 01-233 3000

TREASURY
-3 SEP 1979
P.E.C.S.

C E Henderson Esq.
Department of Energy
Thames House North
Millbank
London SW1

31 August 1979

Dear Charles,

BNOC: DISPOSALS

You and your colleagues came across on Thursday 30 August to discuss the alternative to an outright disposal of BNOC assets as a means of reducing the PSBR in 1979/80, which was set out in your letter to me of 29 August. At the end of the meeting, I promised to reply to your letter setting out the conclusions of our discussion.

We discussed 3 key points of your proposal.

PSBR

The main question of issue was whether the sale in 1979/80 of royalty oil, which would have otherwise accrued in later years, would reduce this year's PSBR. Our conclusion, after consultation with the CSO, was that this transaction was in the nature of borrowing and would only help finance the PSBR, not reduce it. You asked whether this judgement was consistent with the view that the decision earlier this year to take royalty in kind was deemed to bring forward receipts from 1980/81 into this financial year, so reducing this year's PSBR. We pointed out that in taking royalty in kind we were simply exercising an option provided by statute on the method by which government revenues were raised. We were not anticipating tax revenues which would accrue in future years. This differed from the proposal in your letter which was in essence borrowing on the security of future revenues.

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Overseas Debt Management

We then discussed the implications for overseas debt management if the arrangements suggested in your letter followed the model of the Britoil financing. The problem here was that, in contrast to the position when the Britoil deal was made, it is not present government policy to seek further overseas borrowing; the reserves are high and though there may be exceptions, the general concern is to redeem overseas debt, not to raise it. Furthermore HMG (who you pointed out would be the borrower in this case, not BNOC as in the Britoil deal) had consistently declined to offer ~~prejudice~~ PEPGOS or security for its overseas borrowing. We had the highest US credit rating on the strength of the government's own borrowing name and to accede to the sort of proposal outlined in your letter would be to create a most unwelcome precedent for any possible future overseas borrowing.

Domestic Borrowing

Finally we discussed the arrangements referred to in your letter as a vehicle for borrowing in the domestic capital market. Its sole attraction as a way of raising government revenue would be if it could be used to improve the terms on which the government already borrow. It was difficult to see how this could happen. When selling gilts the government benefited from the finest terms available in the market. And such terms were available on the strength of the government's name without the need to resort to the sort of devices referred to in your letter. A departure from borrowing on the strength of the government's name would not be welcome.

We therefore were bound to come to the view that the proposal outlined in your letter would not reduce the PSBR in 1979/80 but would merely finance it. It would be contrary to current overseas debt management policy and it looked to be most unlikely that the arrangements would permit the government to borrow more cheaply on the domestic market than it already can. And with both domestic and overseas borrowing we would in neither case wish to in effect pledge assets or future revenue streams as security for borrowing by HMG.

Yours ever,

Nat Thomas

IAN WICKS

Original in Appts filing

FRIDAY. 2

Prime Minister

We have fixed a meeting with the Howells for Tuesday afternoon.

TL

TO: PRIME MINISTER.

FROM: DAVID WOLFSON.

WHILE IT ISN'T "URGENT", THESE 7/8 DECISIONS WON'T GET ANY EASIER!

DAVID HOWELL WOULD LIKE TO SEE YOU NEXT TUESDAY TO CLEAR A COURSE OF ACTION.

DW

[IT MIGHT ALSO BE USEFUL, IF TIME PERMITTED, TO RECONSIDER THE PRESENT SITUATION ON DISPOSALS?]

SECRETARY OF STATE FOR ENERGY
THAMES HOUSE SOUTH
MILLBANK LONDON SW1P 4QJ
01 211 6402

CONFIDENTIAL

David Wolfson Esq
10 Downing Street

30 August 1979

Dear David

We spoke on the telephone about the chairmanship of BNOC and related matters and I said I would let you have a note as a possible basis for a discussion with the Prime Minister.

My thinking is as follows:

(i) We are not going to get anybody in situ until we have settled firmly the future shape of BNOC, so the sooner we do that the better.

(ii) My own view is that the future BNOC will in effect be two bodies - an oil trading organisation, predominantly existing to carry out Government purposes, and a North Sea oil company which there is no reason for the State to own totally.

I would see the BNOC chairman and main Board as presiding over both wings, with the Deputy Chairman on the main Board being the boss of the North Sea company, in which BNOC would have a 51% shareholding. The remainder of the shares would be spread amongst as wide a range of the public as possible, thus making renationalisation impossible and allowing genuine "public" participation in our North Sea assets.

Against this background I have been looking for two types of person - a figure to chair the BNOC who, while fully equipped for business enterprise would also be very experienced in dealing with Whitehall and Departments and other Governments; and a second figure who would be a top oil man to head the North Sea company.

My suggested candidates for the first role are Sir Francis Tombs or Sir Ronald McIntosh or Ashley Rayburn of Rolls Royce. Sir Francis now chairs the Electricity Council but might be persuaded to move over. Sir Ronald was a Civil Servant and a Director General of the NEDC, and is now with Warburg's. Both are experienced business-like figures who know their way round Whitehall but have a healthy contempt for bureaucracy. I have not met Ashley Rayburn, but he was in Shell and before that the Treasury and Frank McFadzean speaks highly of him. Alternatively I could try and keep on the present Deputy-Chairman Lord Croham (Douglas Allen) as interim Chairman for a year and then try Michael Pocock, who steps down next June, and who would of course be quite excellent.

My first candidate for the North Sea company would be Matt Linning. Mr Linning was responsible at BP for developing the Forties field and is now retired and lives in Aberdeen. He is a first class oil man and widely respected in the industry. Another possibility is Desmond Watkins of Shell.

To support these two posts I would like to change and strengthen the BNOC Board and bring in some people who understand our view point and can give us good advice without maintaining BNOC as the State monstrosity it was becoming. The names I have in mind are Victor Rothschild, Phillip Shelbourne, Tom Boardman, Jeremy Leonard (formely BP), Ronald Grierson (not in any executive role but simply in the same ideas capacity as Arnold Weinstock uses him), and Sir John Greenborough (who will be free next May).

I believe with this sort of group the Government's access to oil policy advice will be greatly strengthened. Naturally I would also dearly like to have Frank MacFadzean on the Board as well, if he would serve.

Of those mentioned so far in this note McIntosh and Linning would, I know, be interested, depending on the precise nature of the posts offered. Grierson has volunteered help. None of the others have been sounded out.

I will be happy to talk to the Prime Minister on these tentative ideas and in particular to know who amongst these she would rule out completely, which would save a great deal of further trouble.

Yours ever

David

7

D A R HOWELL

PECS

6/233/01

CONFIDENTIAL.

DEPARTMENT OF ENERGY

Thames House South, Millbank, LONDON, SW1P 4QJ

Telephone: Direct Line 01-211 4722
Switchboard 01-211 3000

TREASURY
-3 SEP 1979
P.E.C.S

N. Wicks Esq
Treasury
Whitehall
London SW1

PU. R Ward
cc PU C. Ward
PU Gill
PU Thornton
+1

29 August, 1979

Fol discussion tomorrow afternoon.
N.L.W. 29-8

Dear Nigel

BNOC : Disposals

Chris Herzig outlined to you, today, an alternative to outright disposal of BNOC assets, which at first sight would seem to assist the PSBR in 1979/80.

2. The proposal is that the Government should extend the principle established in bringing forward into 1979/80 royalty receipts that would have arisen in 1980/81 by taking Royalty in Kind. This would be done by selling in 1979/80 Royalty oil expected to be available to the Government in subsequent years. By way of illustration a forward sale of £400m in 1979/80 could be discharged by 8 equal deliveries worth £50m in 1981/82, up to 1984/5 together with interest; or the first deliveries could be postponed until 1982/3. The amounts needed would be small in relation to the overall quantities of Royalty oil available to the Government which, on the basis of overall production in 1982/83 of 125 million tons, would be worth some £1.6bn.

r4 of £100

3. This would appear to provide a genuine bringing forward into 1979/80 of Government revenues that would otherwise have accrued in subsequent years, and therefore to diminish the PSBR in 1979/80.

4. BNOC with its experience with the Britoil funding would be able to act for the Government in negotiating such a transaction; fundamental features would be that the obligations would be expressed in money terms (thus retaining to HMG the benefit of any oil price rise), and the freedom to dispose of the oil needed to discharge the obligations at the discretion of HMG. If the Britoil precedent is followed then the money would be raised in the US and the proceeds would be in dollars.

5. The attractions of such a deal would be that it would result in less loss of revenues to HMG in subsequent years than could possibly be the case in the event of disposal of oil producing assets; it could be set up relatively quickly; and it would leave BNOC assets intact allowing for correspondingly more to be raised by the introduction of private capital at a later date.

6. You have agreed to come over to discuss this proposal - both from the PSBR point of view, and that of Government overseas debt management - tomorrow afternoon with Chris Herzig. We would hope to have one of our lawyers present to go over any legal difficulties which might arise.

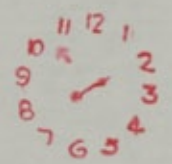
No in HMT.

Yours Sincerely
Charles Henderson.

C.E. HENDERSON

nla

- 4 SEP 1979



SECRET

(24) JS
cc CO
Energy

10 DOWNING STREET

From the Private Secretary

28 August 1979

The Prime Minister has seen the Financial Secretary's minute of 22 August, reporting BP's proposal to split BP stock into 25p units.

She is content that the Financial Secretary should tell Sir David Steel that the Government is agreeable to an announcement on 6 September of the splitting of the BP stock into 25p units provided that the first practical impact day for sale of the stock would then be 24 October.

I am sending a copy of this letter to Martin Vile (Cabinet Office).

M. A. PATTISON

Mrs. P.C. Diggle,
HM Treasury.

SECRET

PRIME MINISTER (23)

Agree that Mr Lawson may approve splitting of BP stock?

MAP 23/VIII

Yes pls.

PRIME MINISTER

BP STOCK SALE

The Chairman of BP, Sir David Steel, has asked our views on a proposal to split the BP stock now denominated in £1 units into 25p units. Subject to his Board's agreement, his plan would be to make an announcemnet of this on 6 September with the operation (which would have to include an Extraordinary General Meeting and Class Meetings of stockholders) being completed on 8 October. This would mean that the first practical impact day (ie day of announcement) for a Government sale of BP stock would be on 24 October. To meet this timetable a decision would be needed by 25 September.

The market price of the £1 BP share now stands at nearly £12 and it is generally agreed that high value shares like theirs are less attractive to small shareholders than shares which stand in the market at a lower price. There may be some element of market folklore about this, but there is undoubtedly something in it. I therefore support the principle of Sir David Steel's proposal, particularly since one result may be to encourage smaller shareholders - including BP employees - to participate in any future stock sale.

The main point at issue for the Government is whether the timetable he suggests would fetter our freedom of action in deciding the impact day for any stock sale. E Committee will consider the question of a BP stock sale next at their meeting on 11 September. If they then decide to proceed with the sale, the earliest possible impact day would still be 24 October since any earlier announcement in October (and perhaps even one on 24 October) is effectively ruled out by the announcement of the results of BP's American subsidiary, Sohio, which is due about that time. I therefore do not see that we would lose anything by agreeing to Sir David Steel's proposal. Subject

to your views, I propose therefore to tell him that the Government is agreeable to an announcement on 6 September of the splitting of the BP stock into 25p units provided that the first practical impact day for sale of the stock would then be 24 October.

I am sending a copy of this minute to Sir John Hunt.

PCS

NIGEL LAWSON
22 August 1979

(Approved by the Financial Secretary and signed in his absence)

23 AUG 1979

FINANCIAL SECRETARY TO THE TREASURY

Energy

Treasury Chambers, Parliament Street, SW1P 3AG

17 August 1979

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

Dear David

INDUSTRY BILL

Thank you for your letter of 3 August about the inclusion of powers for certain disposals in the Industry Bill. I am glad to see that work is already in hand on the provisions required for the Bill in respect of both BNOC and The Radiochemical Centre.

I have noted that you are not seeking at this stage inclusion in the Bill of powers to dispose of BGC assets. I have still to be convinced that it would be wrong to exclude such powers from the Bill, particularly as E(DL) agreed that £400 million net should be raised in 1979-80 from the sale of BNOC and BGC assets. I understand that your present intention is to find the whole £400 million from sales of BNOC assets. Even so, I can still see a case for including a suitable power to dispose of BGC assets in the Bill, particularly Wytch Farm and possibly their offshore oil assets. The disposals exercise is continuing into the next financial year and if BGC do not make a contribution to this year's exercise, I can see no reason why they should not make a contribution to next year's. It would therefore be helpful to have the legislation already enacted on the statute book either by means of the Industry Bill or the Submarine and Pipelines Act (Amendment) Bill. I should be grateful for your views.

I am sending a copy of this letter to the Prime Minister, the Lord President, Members of E(DL) Committee, the Minister of Transport, the Attorney General and Sir John Hunt.

Yours ever
Nigel

NIGEL LAWSON

17 AUG 1979

CONFIDENTIAL

Energy

Nigel

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

Nigel Lawson Esq MP
Financial Secretary
HM Treasury
Parliament Street
London SW1

3 August 1979

Dear Nigel

INDUSTRY BILL

Thank you for copying to me your letter of 16 July to Keith Joseph, on the inclusion of powers for certain specified disposals in 1979/80 in the Industry Bill.

As you know E(DL) has already agreed that legislation enabling me to secure the sale of BNOC upstream assets should be included in the Bill. In the case of TRC we are aiming, in view of the agreement reached at E(DL), to dispose of 100% shareholding, and this will require amendment of the existing legislation which provides for a majority Government stake. I agree that this too should be done through the Industry Bill. My officials will be in touch with Department of Industry officials on the detailed provisions required, in respect of both BNOC and of TRC.

BGC presents a rather more difficult case. Until we are clearer on the exact course to be pursued it would be difficult to draft satisfactory legislation. In addition, I am strongly of the opinion that the inclusion of legislation directed at disposal of specific BGC assets in a published Bill, to be dropped or amended subsequently as our plans are clarified, could prove politically very embarrassing. I am not therefore seeking inclusion of powers to dispose of BGC assets in the Industry Bill at this stage.

I am copying this letter to the recipients of yours.

Yours ever

David

D A R Howell

CONFIDENTIAL

- 3 AUG 1979

Published Papers

The following published paper(s) enclosed on this file have been removed and destroyed. Copies may be found elsewhere in The National Archives.

House of Commons Hansard
26 July 1979, columns 891-902
"Oil Policy"

Signed C M Wayland Date 16 September 2009

PREM Records Team

SECRETARY OF STATE FOR ENERGY
THAMES HOUSE SOUTH
MILLBANK LONDON SW1P 4QJ
01 211 6402

2 26/7

Tim Lankester Esq
Private Secretary to the
Prime Minister
10 Downing Street

26 July 1979

Dear Tim

I attach a copy of the final version of this statement. It is as agreed between the Prime Minister and my Secretary of State, except that in para 7, "BNOC should no longer have a seat on every Committee operating the North Sea*" has been altered to "BNOC should no longer sit on every committee", which may in some cases save the labour and expense of renegotiating the operating agreements.

I am copying this letter and enclosures to the Private Secretaries of members of E Committee and of the Chancellor of the Duchy of Lancaster, the Chief Whips in the Commons and in the Lords, the Paymaster General and the Secretaries of State for Scotland and Wales; also to the Chief Press Officer at No 10 and to Martin Vile.

Yours sincerely,
John Arnott

John Arnott
Private Secretary

* Fields

STATEMENT ON OIL POLICY BY SECRETARY OF STATE FOR ENERGY

With permission, Mr Speaker, I will make a statement about the Government's oil policy and the British National Oil Corporation.

2. The Government has reviewed the full range of the BNOC's activities. It has also had much in mind the serious decline in offshore activity.

3. After discussions with the Chairman and the BNOC Board, the Government has concluded that BNOC can best serve the nation's interests in a continuing but much more limited role than at present, and that the pattern of ownership of the Corporation's assets, at present exclusively in State hands, should be changed.

4. The House will be aware that the BNOC is engaged in two main activities. It is an oil trader on a large scale, mainly by virtue of its right through participation agreements with other oil companies to purchase 51% of most of the oil produced on the UK Continental Shelf. And it has a substantial enterprise in the North Sea, engaged in exploration, development and production.

5. As far as the trading activity is concerned, the Government has decided that the Corporation's access to oil through the participation options should be retained. Although in conditions of major shortage I can take powers under the Energy Act 1976 to control and direct oil movements, in conditions of limited shortage, such as we are now experiencing, BNOC's direct access to 'participation' oil, together with royalty oil, strengthens our position. Of course, quantity and thereby security of supply also depends on economic pricing, and that is why we have removed the price controls which we inherited.

6. As to BNOC's offshore assets and interests, the Government believe that those should be more widely owned. This objective can best be achieved through the disposal of assets from State hands or by the introduction of private capital into the operation. I will be making a further announcement in due course.

7. Furthermore, the Government has decided on a number of steps in the area of BNOC's exploration, development and production activities.

The Corporation has too many licence obligations and commitments, along with a number of privileges vis-a-vis other oil companies. These features are themselves a source of the instability and lack of confidence that have come to characterise the offshore oil exploration scene - which it is essential for us to change. The Government has decided, therefore, that BNOC's preferential position in future licensing Rounds should be ended, and that its present over-extended exploration commitments should be reduced. The Government also intends to end BNOC's special access to Government finance though the National Oil Account. These changes follow the Chancellor's announcement that BNOC will be liable to PRT in common with other oil companies, and my announcement ending the previous policy of giving BNOC a first refusal whenever an interest was assigned between companies. I have also decided that the Corporation's statutory role as adviser to the Government should be removed, and that the Corporation should no longer sit on every committee operating the North Sea fields where it has no equity stake. I shall be strengthening my Department's resources so as to ensure that the Government, in the exercise of its regulatory role, is fully able to protect vital national interests.

8. Some of the changes I have outlined will require legislation, which will be introduced later in the session.

9. The moves announced today will in themselves encourage companies to explore more widely and to invest more confidently in development. We must encourage more investment both in drilling on already licensed territory and in deeper waters on the UKCS. Our decision to examine with the industry the problems of the so-called marginal fields should also be of positive help.

10. In addition I am today confirming the first batch of awards of licences under the Sixth Round (and the announcement of further awards will follow shortly). I am also well advanced with the preparation of a 7th Round of licensing.

11. I believe that all this will make a major contribution to restoring a high level of exploration activity on the UKCS after the recent very serious slow-down.

28 JUL 1978

SECRETARY OF STATE FOR ENERGY
THAMES HOUSE SOUTH
MILLBANK LONDON SW1P 4QJ
01 211 6402

P.2077

A.C. Pirie Esq
Private Secretary to the
Chief Secretary
HM Treasury
Whitehall

21 July 1979

Dear Alistair,

Thank you for your letter earlier today. My Secretary of State has seen the amendments which the Chief Secretary proposes.

On the first point he feels that any of the options which have been considered would indeed result in a widening of ownership, and the recasting proposed is not therefore necessary.

The second and third points are aimed at clarifying that there is no intention of relinquishing the right to take 51% of the oil produced. He agrees that this should be made clear, and will be happy to do so to the extent required in the supplementaries.

The fourth point is covered in the final draft, circulated today under cover of a letter to Tim Lankester.

I am copying this letter to the Private Secretaries of members of E Committee and of the Chancellor of the Duchy of Lancaster, the Chief Whip and the Paymaster General; also to the Chief Press Officer at No 10 and to Martin Vile.

Yours sincerely,
John Arnott

John Arnott
Private Secretary

26 JUL 1979

R
2617

Treasury Chambers, Parliament Street, SW1P 3AG

John Arnott Esq
Private Secretary to
the Secretary of State
Department of Energy
Thames House South
Millbank
London SW1P 4QJ

26 July 1979

Dear John,

DRAFT STATEMENT ON OIL POLICY BY SECRETARY OF STATE FOR ENERGY

Thank you for sending me a copy of your letter to Tim Lankester of 25 July with which you enclosed a copy of Mr Howell's proposed draft statement on oil policy.

The Chief Secretary is broadly content with the statement but there are a number of drafting changes which he would like to see made.

As it stands the first sentence of paragraph 6 is something of a hostage to fortune. Sales of £400 million of BNOC assets to BP could hardly be regarded as ensuring that BNOC's assets are more widely owned. This particular sentence should therefore be dropped. It would then make sense to combine the remaining part of paragraph 6 with what is said in paragraph 3 along the following lines:

> ".....and that the pattern of ownership of the Corporation's assets, at present exclusively in State hands, should be reviewed. We are considering ways in which the Corporation's assets might be disposed of to the private sector or in which private capital might be introduced into their operations. I shall let the House know our conclusions in due course."

The fourth sentence of paragraph 7 of the proposed statement is ambiguous and could be read as going further than we intend. The idea of the "preferred position in future licensing rounds" could be seen as embracing not only BNOC's automatic equity participation (which it is proposed to give up) but also the right to purchase 51 per cent of the oil produced (which it is not proposed to give up). To make this clear the sentence should be modified to read:

"... preferred position in relation to equity participation in future licensing rounds."

In view of the fact that we are intending to hold on to the rights to purchase 51 per cent of the oil produced the start of the third sentence of paragraph 7 should be amended to read:

"We regard some of these features....."

The final sentence of paragraph 7 refers to the strengthening of the Department's technical resources. Does this mean that you have either sought and obtained the approval of the Civil Service Department for any increase in staff involved or that you propose to find the costs of any additional staff from within your existing cash limits and PES approval?

Paragraph 10 of the statement says that details of a Seventh Round of Licensing will be announced "as quickly as possible". The minutes of the sixth meeting of E Committee make it clear that decisions on the extent, nature and timing of the Seventh Round Licensing will not be taken until the Committee has considered future oil depletion policy. The paper on this subject will not be coming forward until the Autumn and in the circumstances it would be preferable to change the form of words from "as quickly as possible" to "in due course".

I am copying this letter to the recipients of yours.

Yours sincerely,

Alistair Pirie

A C PIRIE
(Private Secretary)

26 JUL 1979

1

Mr Howell has approved the amendments

SECRETARY OF STATE FOR ENERGY
THAMES HOUSE SOUTH
MILLBANK LONDON SW1P 4QJ
01 211 6402

Tim Lankester Esq
Private Secretary to the
Prime Minister
10 Downing Street

25 July 1979

Dear Tim,

PARLIAMENTARY STATEMENT ON BNOC

It was agreed at E Committee yesterday that my Secretary of State should recirculate the draft of the statement on BNOC which he proposes to make on Thursday, amended to reflect the decision not to press ahead at once with the announcement of a seventh round of licensing. This is now attached, and my Secretary of State will be grateful for comments. The Statement is in the timetable for 3.50 on Thursday and he would hold a press conference later that day.

I am copying this letter and enclosures to the Private Secretaries of members of E Committee and of the Chancellor of the Duchy of Lancaster, the Chief Whip and the Paymaster General; also to the Chief Press Officer at No 10 and to Martin Vile.

Yours Sincerely
John Arnott

John Arnott
Private Secretary

N.B. Ken Berrill thinks this is O.K.

TL.

PRIME MINISTER

We have ended up with this and the disposal statement tomorrow - a combination which will appeal to the Opposition.

Have you any comments on Mr Howell's draft?

MJS
25/VII

Prime Minister PA 1

This seems alright: it closely follows E Committee's conclusions yesterday and Ken Berrill thinks it is OK. Are you content?

25/7

SECRETARY OF STATE FOR ENERGY
THAMES HOUSE SOUTH
MILLBANK LONDON SW1P 4QJ
01 211 6402

Tim Lankester Esq
Private Secretary to the
Prime Minister
10 Downing Street

25 July 1979

Dear Tim,

PARLIAMENTARY STATEMENT ON BNOC

It was agreed at E Committee yesterday that my Secretary of State should recirculate the draft of the statement on BNOC which he proposes to make on Thursday, amended to reflect the decision not to press ahead at once with the announcement of a seventh round of licensing. This is now attached, and my Secretary of State will be grateful for comments. The Statement is in the timetable for 3.50 on Thursday and he would hold a press conference later that day.

I am copying this letter and enclosures to the Private Secretaries of members of E Committee and of the Chancellor of the Duchy of Lancaster, the Chief Whip and the Paymaster General; also to the Chief Press Officer at No 10 and to Martin Vile.

Yours sincerely
John Arnott

John Arnott
Private Secretary

DRAFT STATEMENT ON OIL POLICY BY SECRETARY OF STATE FOR ENERGY

With permission, Mr Speaker, I will make a statement about the Government's oil policy and the British National Oil Corporation.

2. ~~Over the last few weeks~~ the Government has ~~carefully~~ reviewed the full range of the BNOC's activities. It has also had much in mind the serious decline in offshore activity. I have had several discussions with the Chairman and I have also met the BNOC Board. I pay tribute to the dedication of the Corporation's management and staff.

3. The Government has concluded that BNOC can best serve the nation's interests in a much more limited role than at present, and that the pattern of ownership of the Corporation's assets, at present exclusively in state hands, should be changed.

4. The House will be aware that the BNOC is engaged in two main activities. It is an oil trader on a large scale mainly by virtue of its right through participation agreements with other oil companies to purchase 51% of most of the oil produced on the UK Continental Shelf. And it is itself a substantial enterprise in the North Sea, engaged in exploration, development and production.

5. As far as the trading activity is concerned, the Government has decided that the Corporation's access to oil through the participation options ~~can still play a useful part in guaranteeing the UK's security of oil supply, and~~ should be retained. Although in conditions of major supply shortfall I can take powers under the Energy Act 1976 to control and direct oil movements, in conditions of ~~any~~ limited shortage, such as we are now experiencing, BNOC's direct access to 'participation' oil, together with royalty oil, strengthens our position. Of course, security of supply also depends

is it quantity that depends on pricing — not security?

on economic pricing, and that is why we have removed the price controls which we inherited. But in a changing and precarious world oil situation I believe that it is right for a Government body to be involved in the trading of oil. This has been said in more acceptable form previously — after which we would not argue with, and we would welcome.

6. As to BNOC's offshore assets and interests, the Government believes that these should be more widely owned. ~~I intend to give the House further details of my plans in this respect in due course. We are considering how~~ this objective could be achieved through the disposal of assets from State hands or by the introduction of private capital into the operation. B.P. in Alaska.

But we are committed to sell some fields

7. Furthermore, the Government has decided on a number of steps in the area of BNOC's exploration, development and production activities. The Corporation has too many licence obligations and commitments, along with a number of privileges vis-a-vis other oil companies. These features are themselves a source of the instability and lack of confidence that have come to characterise the offshore oil exploration scene - which it is essential for us to change. The Government has decided, therefore, that BNOC's ~~preferred~~ preferential position in future licensing Rounds should be ended, and that its present over-extended exploration commitments should be reduced. The Government also intends to end BNOC's special access to Government finance though the National Oil Account. These changes follow the Chancellor's announcement that BNOC will be liable to PRT in common with other oil companies, and my announcement ending the previous policy of giving BNOC a first refusal whenever an interest was assigned between companies. I have also decided that the Corporation's statutory role as adviser to the Government should be removed, and that the Corporation should no longer ~~exercise its right to~~ have a seat on every committee operating the North

those committees operating the North Sea Oil fields where it has an equity stake.

Sea fields. I shall be strengthening my Department's resources so as to ensure that the Government, in the exercise of its regulatory role, is fully able to protect vital national interests.

8. Some of the changes I have outlined will require legislation, which will be introduced later in the session.

9. The moves announced today will in themselves encourage companies to explore more widely and to invest more confidently in development. We must encourage more investment both in drilling on already licensed territory and in deeper waters on the UKCS. Our decision to examine with the industry the problems of the so-called marginal fields should also be of positive help.

10. In addition I am today confirming the first batch of awards of licences under the Sixth Round (and the announcement of further awards will follow shortly). I am also well advanced with preparations for a 7th Round of licensing.

11. I believe that all this will make a major contribution to restoring a high level of exploration activity on the UKCS after the recent very serious slow-down.

25 JUL 1879

Mr Jenkins, M. Younger + R. Channon just walked in before item (disposal) was reached.

I think I ought to say that what they have heard about disposal of assets is very sensitive commercially + they ought therefore not to discuss it with anyone else

Ref: A029

CONFIDENTIAL

PRIME MINISTER

Future of BNOC
(E(79) 20, 21, 22 and E(DL)(79)6)

BACKGROUND

There are no new circulated papers for this meeting, but you will want to read again the Secretary of State for Energy's minute of 18th July; the Chancellor's comment on this dated 19th July; the Chancellor's minute of 20th July reporting discussion in E(DL); and the Attorney General's minute of 20th July. The Foreign and Commonwealth Secretary, who is in Brussels with the Lord Privy Seal, has also recorded his views (minute of 23rd July).

2. Following the discussion in E on 17th July, there have been a number of bilateral talks, and a meeting of E(DL) on 19th July. As a result of the latter, the Attorney General held private talks with BP's lawyers, reported in his minute. The Ministers concerned are meeting again under the Chancellor's chairmanship on Monday afternoon 23rd July. In addition, there was some brief discussion of these points at your Monetary Seminar on 18th July.

3. Decisions are now needed in four related areas:-

(i) The future role of BNOC, and the first steps on dismantling the Corporation.

(ii) The sixth round of licensing.

(iii) Disposal of BNOC assets, this year and later (and possibly also sale of BGC assets).

(iv) Disposal of BP shares.

HANDLING

4. You might take each of these in turn:-

(i) The future role of BNOC. Mr. Howell's proposals are set out in E(DL)(79) 6, and in his minute of 18th July. You might take the three main functions in reverse order of difficulty:-

(a) Advisory Role. Mr. Howell wants to scrap this, and to remove BNOC from the operating committees. One oil company has recently described BNOC's presence on these committees as 'like having the camp commandant sitting in on the escape committee'. But the Chancellor sees some value in continued BNOC membership. It provides a source of information on pricing; costs; and oilfield development. It is worth remembering that the two proposals do not necessarily hang together. BNOC could lose its role as statutory adviser to the Government and still retain membership of the operating committee if advantage were seen in this course.

(b) Participation. Assuming at least some reduction in BNOC's up-stream role, continuation of the participation agreements is central to a continued trading role for BNOC. It is argued that this trading role gives the Government greater control over the disposition of oil in an emergency. Your own view so far has been against continuing the participation agreements. It is also relevant that the way in which they were obtained was doubtfully legal under Community Law: although in practice it has never been attacked. However, the majority of the Ministers consulted (notably the Chancellor, the Secretary of State for Energy and I think also the Lord Privy Seal) think this function should continue. Incidently, although it is alleged that BNOC has compounded our oil supply difficulties by excessive export of oil, BP exported half as much again in the first half of 1979. And BNOC, unlike BP, has rapidly unwound its export commitments, entered into earlier in the interests of getting the best price for the Treasury.

(c) Upstream. It is common ground that some at least of the upstream equity interests should be sold: the question is one of degree. Mr. Howell argues that to go too far will emasculate the Corporation. It will no longer be a credible trading partner.

There is a case, which the Foreign and Commonwealth Secretary might have deployed were he present, for retaining some exploration and development capacity for 'strategic' purposes - e.g. to block French ambitions in the disputed South Western approaches, or to explore and then sterilize prospective oilfields in the interests of depletion policy. These arguments would point against a block sale to BP. In addition, some of your colleagues may doubt whether BP could or would play this 'chosen instrument' part. To do so would carry some risk to its credibility as an independent multi-national and the company has always fought shy of identification with the British Government. Moreover membership of the EEC rules out overt direction of BP on oil supply quite apart from the Government's self-denying ordinance in the shape of theBradbury/Bridges correspondence.

It should now be possible to reach a final decision on these three points, in order to allay uncertainties and allow planning to go forward. In that case, a number of secondary points arise:-

(d) Establishment of a Subsidiary Company. Mr. Howell proposes this (minute of 18th July) and the Chancellor sees no serious difficulty (19th July). It was originally proposed as a first step towards the introduction of private capital. It would go equally well with a block sale to BP (although it would not help with the 'pre-emption' problem - see below). It would not facilitate, and might slightly complicate, the task of a partial disposal: although presumably a subsidiary company could just as easily sell a limited number of assets as could the parent corporation.

(e) The Chairman. Lord Kearton has made it clear that he wants to go quickly. Any potential successor will need to know the size of the job he is taking on. It may also affect the appropriate level of salary. (Kearton does not draw his.) It will not be

possible to announce a new chairman before the Recess: but early steps should be taken about selection. You may want to pursue this separately after the meeting.

(f) Public Announcement. If agreement can be reached on the main points above, there is every advantage announcing it early. It would help with the presentation of the sixth round decision - see below. It would also provide a framework for the disposals package. But - on the Attorney's advice - it will be important not to announce in advance the destination of the assets.

(ii) Sixth Round Licenses. If BNOC is to have no major continuing upstream role, it is common ground that it need not be given any further licenses - at least at present. The preferred option is therefore to grant the sixth round licenses which have already been allocated in principle; to let BNOC take up temporarily the rights which these licenses grant them (because this is the basis on which applications have been made, and the Attorney advises that to change them at this late stage would involve retrospection) and to disentangle BNOC from each license separately as soon as possible thereafter. The Chancellor, the Secretary of State for Energy and the Attorney all prefer this course. The alternative would have been to hold up the allocation of this extra licenses, at some risk of delay to the development of the North Sea. But allocation in this way involves some explanation of why BNOC is still involved. It might be possible to make a holding statement, that BNOC's future role was still under consideration: but it might equally be preferable to put this into a broader context by announcing decisions on the future of the Corporation - as above. No decision need be taken or announced at this stage about the seventh round, which Mr. Howell mentions (18th July): this will raise important questions of depletion policy to which the Committee should return in the autumn. Similarly his request in a separate minute to you of 20th July to announce a new approach to licensing policy should await the Committee's consideration of depletion strategy.

(iii) Disposal. There are, as the Chancellor says in his minute of 20th July, three packages available, though they overlap to a degree (e.g. even full disposal to BP leaves a gap to be covered by the sale of BP shares if the full £1 billion is to be obtained).

(a) Complete Disposal to BP. Sir David Steel has told you that he is prepared to buy the lot. He would like to do so by taking up shares in a subsidiary. But this may have been based on mistaken advice. The Attorney General (letter of 20th July) does not believe this will help resolve the 'pre-emption' problem. There seems little alternative to negotiating away separately the existing rights of some 35 partners, some of whom may very well object to an enlarged role for BP. (Paradoxically, they prefer the less-powerful BNOC as a partner). There would be difficult problems of valuation, though these are not unprecedented. Some form of reference to independent arbitration might be necessary. The net yield could well be less than the purchase price, because of the need to net off the Government's share of any future rights issue: alternatively, the Government would prejudice its ultimate control of BP. The net benefit to the PSBR might be smaller still, because of the effect on BP's tax liabilities: these have yet to be worked out in detail. BP would require a formal reaffirmation of the 'Bradbury/Bridges' relationship, which would be publicly difficult to reconcile with the continued control over disposal of oil. It might not be possible to complete the transaction in the present financial year: but the 'seminar' thought that provided the deal were agreed in principle, and a substantial down-payment made, this need not necessarily matter.

(b) The smaller disposal package. The fields involved, in order of preference, are Viking, Statjford, Dunlin, Murchison & Ninian (or part). The Attorney has confirmed that all of these raise 'pre-emption' problems. (In the case of Ninian, these do not arise if the disposal is part of a total package: but that does not help much). Still, the chances of negotiating ones way out of the limited number of agreements in a limited time must be better than that of the total package. You might ask whether creation of a subsidiary company would make this route any more difficult? (Probably not). Mr. Howell will also argue that disposal on this scale, while still leaving BNOC with upstream liabilities, will turn it into a loss-maker. This is a question of timing, not of substance: Her Majesty's Government would be bringing forward, in the form of a capital payment, the future cash flow from the fields disposed of: the 'losses' would in fact be BNOC's share of future investment in its continued fields, which would in due course yield additional revenue. In any case, his objection applies with much less force to the sale by BGC of Wytch Farm; you might try to reinstate this in the smaller package. He has argued that BP do not want it (for fear of complicating their relations with BGC) but there is no reason why Shell should not take it on: or it be sold to a city consortium established for the purpose.

Either course needs legislation. The Committee should therefore confirm policy approval for statutory powers to direct BNOC to divest itself of substantial parts of its assets. These clauses can be added to the Industry Bill, being introduced shortly after the Recess. No such powers are needed to direct BGC to sell Wytch Farm.

(iv) BP Shares. Even if the decision has been to risk the 'whole hog' sale to BP, there will still be a short-fall on the Chancellor's original £1,000 million. You will not want to take a final decision at this stage on the extent of the sale of BP shares which may be needed. Equally,

you will not want, I suggest, to let the chance of selling BP shares go by default. The Bank of England advice is that even a partial sale of the present BP holding will get a better price if payment is received in two tranches at 3-month intervals. Leaving some margin for market manoeuvre, the latest date for the offer is therefore about end-October: and several weeks' preparation are involved. You might be prepared to authorise the Chancellor to proceed, so far as can be done without public disclosure, with the preparation for such a sale. There are then a number of subsidiary questions, about the allocation to existing employees and to small shareholders, which could be left to him and the Financial Secretary: the Committee's general intentions on these points are already well known. If necessary, this Committee, or E(DL) could look again at any remaining problems (e.g. sales to foreign investors) in September, before any public action is needed. You will want to reserve the final decision on the sale for your own consideration.

CONCLUSIONS

5. I suggest you aim to record conclusions on the four main points above:-

(a) The future role of the Corporation, including its advisory role, its participation/trading role; and the extent of its upstream involvement; the creation of its subsidiary company; the selection of a new chairman and a need for a statement.

(b) Sixth round: whether or not to go ahead with the present allocation, and what sort of announcement to make.

(c) Disposal: whether to go by the "sale to BP" route, or with the smaller package, and if so, the content of a smaller packet; in either case, confirming policy approval for legislation

(d) Keeping open the option of selling BP shares by instructing the Chancellor to proceed with preparations for a possible sale.

(John Hunt)

23rd July, 1979

Prime Minister 22

For E Committee

SECRET

Qa 04206

To: MR LANKESTER

From: SIR KENNETH BERRILL

23/7

North Sea Oil and Gas: Security of Supply

1. The Government is unfortunately faced with the need to meet the bulk of its £1bn. sale of assets in the financial year 1979/80 by the sale of some combination of BP shares and BNOC/British Gas assets in the North Sea. There are many facets to this difficult choice but an important issue is the effect of the decision on security of supply of oil and gas to the United Kingdom market.

BP Shares

2. As far as security of supply is concerned, it has to be recognised that ownership of BP shares is virtually irrelevant. BP regards itself as a multinational company (only 15 per cent of its activity is in the UK market) but more than this it is always preoccupied with the need to demonstrate that it is independent of the UK Government. The interpretation of the 'Bradbury letter' which has been followed for many years has made the British Government's holding of BP shares non-operational from this point of view. BP have managed to get British Governments to say publicly that they do not interfere in the commercial operations of the company. (It is argued that this declaration is required by the Securities and Exchange Commission if BP share issues are to be offered in New York.) BP lose no opportunity to try to get British Governments to repeat that assurance. But, more than this, in practice their determination to achieve an arm's length relationship means that often it is easier to persuade an American company (e.g. Texaco or Esso) to favour the UK market in their supply policy than it is for a British Government to persuade BP.

BNOC

3. The Government of every country which produces oil and gas in substantial quantities does its best to ensure preference for its own market. This is not necessarily achieved by nationalisation. But where, as in North America, there is no Government ownership, there is instead an extremely detailed bureaucratic control.

4. In Canada there are two levels of control: the State control in Alberta (80 per cent of Canadian output) and the Federal control. The control is very detailed (well by well, period by period). In the United States the bureaucracy is so complex that it covers output, pricing and movement of oil and gas inside the United States.

5. The control of exports is a prime requirement of both the Canadian and American system. The Americans allow no export at all and require all the Alaskan production to be brought down to the mainland US even though the natural destination for Alaskan production would be Japan. Here in Britain we would not like to see the complex bureaucracy which is in part responsible for the regional shortages of oil products which have plagued the United States. But the fundamental point is that we have to operate within the constraints of membership of the EEC which would not allow us to institute the detailed and overt export controls which exist in North America. So there is more than just convenience in having a BNOC as part of our control mechanism: it enables the Government to keep within the EEC rules by distancing itself from the control operations. Also BNOC can, given time, recruit 'oil men' in a way in which it would be difficult for a Government Department.

6. 'Knowledge is power' and to some extent the ability of the Government to achieve security of supply (and an adequate tax take) depends on its knowledge of what is going on in the oil and gas fields. This cannot be achieved by operating only as an oil and gas 'trader'. There is a great deal to be said for the British authorities (BNOC) retaining a seat on all the Operating Committees. The oil companies will not like this - one

oil executive is said to have described the situation as equivalent to 'having the Camp Commandant on the Escape Committee'. But that very resistance is an indication of the importance from the Government's point of view of keeping both this crucial source of information and oil experts on their pay roll capable of interpreting it.

Conclusions

7. From a strictly 'security of supply' viewpoint, it would be preferable to sell BP shares rather than to transfer BNOC oil to BP because in the past BP has proved less amenable to the UK Government's pressure than any other major oil company. Apart from this, the Government will need to retain a machinery to monitor and influence the destination of North Sea oil and gas and, given our membership of the EEC, operating through BNOC is the only route we have.

8. Membership of the Operating Committees of each field is a very important source of information which cannot be achieved by keeping a purely trading function.

9 I am sending a copy of this minute to Sir John Hunt.

KB

23 July 1979

21

SECRET

PM/79/69

PRIME MINISTER

BNOC: FUTURE STRATEGY AND DISPOSAL OF ASSETS

1. Since I shall be in Brussels on 24 July for the Foreign Affairs Council I shall not be able to attend E Committee that day. I am therefore writing to put on record my views on the proposals in David Howell's minute to you of 18 July, in the light of Geoffrey Howe's minute of 19 July and of the fact that E (DL) on 19 July apparently reached no decision on recommendations to E on these issues.

2. The control over a substantial amount of North Sea oil which we derive from BNOC's upstream assets is in my view more secure and less controversial internationally than our control over North Sea oil traded by the multinationals, including BP; and for that reason it is important for our future security of supply. I therefore agree with David Howell that the question of disposal of BNOC's upstream assets, whether by a partial sale or a total takeover of these by BP, must be looked at very carefully and should not be rushed. At the same time I agree with him that we ought to make a statement on future policy towards BNOC before the recess, particularly to enable work under 6th round licences to go ahead. I believe that David Howell's proposals offer a good basis for such a statement, while not prejudicing the question of how much of BNOC's upstream assets should eventually be disposed of, and to whom.

3. I am copying this minute to the other members of E and E (DL) and to Sir John Hunt.

C

Foreign and Commonwealth Office
23 July 1979

(CARRINGTON)

SECRET

23 JUL 1979

CONFIDENTIAL

PRIME MINISTER

DRAFT STATEMENT ON OIL POLICY

Ahead of 'E' I thought it would be helpful to circulate the draft of a Statement on Oil Policy, I have in mind for Thursday.

In my view to make this Statement at this particular moment, will make a major and immediate contribution to accelerating the North Sea and linked investment we so badly need, without unduly raising the Parliamentary temperature and without in any way foreclosing the options we shall wish to exercise on the financial side later in the year.

I am copying this minute to Members of 'E' Committee and to Sir John Hunt.

DH.

Secretary of State for Energy
23 July 1979

CONFIDENTIAL

DRAFT STATEMENT ON OIL POLICY

With permission, Mr Speaker, I will make a statement about the Government's oil policy and the British National Oil Corporation.

2. Over the last few weeks the Government has carefully reviewed the full range of the BNOC's activities. I have had several discussions with the Chairman and I have also met the BNOC Board. I pay tribute to the dedication and sense of public service of the Corporation's management and staff, which will I am sure continue.

3. As the House knows, the Government was elected with a commitment to devise policies which would stimulate again the exploration and production of our oil and gas resources, and to reduce the degree of State involvement in those activities. Consequently, the Government has concluded that BNOC should now play a substantially reduced role, and that the basis of the Corporation's ownership should be broadened.

4. The House will be aware that the BNOC is engaged in two distinct areas of activity. It is an oil trader on a very large scale, mainly by virtue of its right through participation agreements with other oil companies to purchase 51% of most of the oil produced on the UK Continental Shelf. And it is itself a substantial enterprise in the North Sea, with very extensive interests in exploration, development and production.

5. As far as the trading activity is concerned the Government has decided that the Corporation's access to oil through the participation options can still play a part in guaranteeing the UK's security of oil supply, and should be retained. Although in conditions of major supply shortfall I can take powers under the Energy Act 1976 to control and direct oil movements, in conditions of more limited shortage, such as we are now experiencing, BNOC's direct access to 'participation' oil, together with royalty oil, strengthens our position. I put it no higher than that since security of supply will also depend on maintaining economic pricing now that we have removed the price controls which we inherited. But in a changing and precarious world oil situation I believe that it is right for a Government body to retain this function.

6. As far as BNOC's exploration, development and production role is concerned, the Government has decided on a number of steps. The Corporation has been given or acquired far too many licence obligations, along with a number of privileges vis-a-vis other oil companies. These features are themselves a source of the instability and lack of confidence that have come to characterise the offshore oil exploration scene - which we must reverse. The Government has decided, therefore, that BNOC's preferred position in future licensing Rounds should be ended, and that its present over-extended exploration commitments should be reduced. The Government also intends to end its special access to Government finance though the National Oil Account. These changes follow the Chancellor's announcement that BNOC will be liable to PRT in common with other oil companies, and my announcement ending the previous policy of giving BNOC a first refusal whenever an interest was assigned between companies.

I have also decided that BNOC's statutory role as adviser to the Government should be removed, and that the Corporation should no longer exercise its right to a seat on every committee operating the North Sea fields. I shall be strengthening my Department's advisory resources so as to ensure that the Government is fully able to protect vital national interests without being dependent on outside advice.

7. The Government believes that BNOC's offshore assets and interests should be more widely owned. We are therefore considering ways both in which assets can be disposed of to the private sector, and in which private capital can be introduced into the operation. I shall give the House further details of these plans in due course.

8. Some of the changes I have outlined will require legislation which will be introduced later in the session.

9. The moves I have announced will in themselves encourage companies to explore more widely and to invest more confidently in development. We must encourage more investment both in drilling on already licensed territory and in deeper waters on the UKCS. Our decision to examine with the industry the problems of the so-called marginal fields should also help here. In addition I am today confirming the first batch of awards of licences under the Sixth Round (and the announcement of further awards will follow shortly).

10. I am also today announcing the Government's plans for future licensing and details will be given in a written answer. These involve immediate preparation of a 7th Round of licensing and a new policy for the more rapid licensing of new territory in the longer term. I believe that all this will make a major contribution to restored high exploration activity on the UKCS after the recent slow-down.

SECRET

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

PRIME MINISTER

BNOC : FUTURE STRUCTURE AND DISPOSAL OF ASSETS

As you asked us, E(DL) considered this afresh last night in the light of further advice from the Attorney General. We also had before us the Secretary of State for Energy's minute to you of 18th July and my commentary of 19th July.

2. We reached no final decisions, which must of course be subject to further discussion in E on Tuesday, 24th July.

3. I need not recapitulate the whole discussion. Three major new points have emerged:

(i) the Secretary of State for Energy would, as a first step, like to float off the up-stream assets of BNOC into a subsidiary company. (His minute of 18th July contains this suggestion). This would be a preliminary, either to his own initially-preferred course of selling shares to the general public; or alternatively, to the sale of some or all of the shares to BP;

(ii) this is BP's preferred solution too. They believe that it would allow the transfer of assets to them to take place without giving the right of first refusal to the other partners in the field concerned;

(iii) the Attorney General disagrees. He has only had a chance to consider very quickly the agreements

SECRET

governing the seven prime targets for disposal. But it is already clear that there are entrenched rights, of first refusal and in some cases of absolute veto, which will have to be negotiated away with each individual partner. (There are some thirty-five companies involved in the present commercial fields in which BNOC has an interest.) He does not consider that the subsidiary company device would successfully avoid these obstacles. He considers that it could probably be challenged in the Courts, but is prepared to reconsider this advice in the light of discussions he will be having in the next day or two with BP lawyers.

4. The Sub-Committee therefore agreed:

(a) to invite the Attorney General to conduct these talks with BP urgently and in strict confidence, and to report back to E on Tuesday;

and, subject to the views of E:

(b) that there was no objection to the sixth round licensing going forward on the basis preferred by the Secretary of State for Energy and the Attorney General - i.e. with the initial involvement of BNOC, which would be renegotiated case by case once the licenses had been issued;

(c) that the Secretary of State for Energy would have to make an announcement about these licenses, making it clear that the inclusion of BNOC did not imply that BNOC necessarily had a continued up-stream role, and that the whole question of its up-stream involvement was still under consideration; (he himself would like to go further, and to announce the outcome of the review, on the lines he suggests in his minute to you

of 18th July);

(d) that BNOC should be invited to form a subsidiary company to which its up-stream assets should be transferred, and (possibly) that this intention should be announced at the time that the sixth round licensing decisions are announced;

(e) that legislation be introduced in the next Session (in practice, as additional clauses added to the Industry Bill) to permit the Secretary of State for Energy to direct BNOC to dispose of its assets in this way (the Attorney General having advised that such legislation is essential);

(f) that the main options on disposal remain:

(i) the sale of all the up-stream assets of BNOC to BP; this option is only open if the Attorney General can remove the legal doubts about the subsidiary company route; or if it is a practical proposition to negotiate with all thirty-five licensees in time to complete the sale by 1st April; this course would require BP to make a large rights issue, and this in turn means either that HMG's holding would come down to about 42 per cent, or that it took up its share of the rights and thus fell short of the £1,000 million target;

(ii) to dispose of part of the up-stream assets of BNOC (and possibly also of BCG's Wytch Farm field), leaving the remainder of the desired total to be found by a limited sale of BP shares; or

(iii) to abandon as impracticable the sale of BNOC assets in the current year, and to make preparations for the early sale of up to £600 million worth of BP shares.

5. I am sending copies of this minute to the Secretaries of State for Energy, Industry, Trade, Environment and Scotland; to the Lord Privy Seal; to the Attorney General; to the Chief Secretary and Financial Secretary, Treasury; and to Sir John Hunt.

[Approved by the Chancellor of the Exchequer and signed in his absence] M E Hall (G.H.)

20 July, 1979

SECRET

P 2

ROYAL COURTS OF JUSTICE
LONDON, WC2A 2LL

01-405 7641 Extn 3201

20 July 1979

The Rt Hon David Howell MP
Secretary of State for Energy
Department of Energy
Thames House South
Millbank
LONDON S W 1

Prime Minister

R
23/7

Dear David,

DISPOSAL OF ASSETS BY BNOC

At E(DL) yesterday the possibility was discussed that BNOC might transfer its upstream assets to a wholly-owned subsidiary and then arrange for a sale of all the shares in that subsidiary to BP. In this way, it has been said, the pre-emption and other restrictive conditions on sale by which BNOC is bound under various UKCS agreements would not have to be observed. This course has been described as the "corporate route".

Today I had a meeting with the Legal Adviser to BP and we went over the ground with lawyers from your Department. Treasury Counsel was also present. It turned out that Mr Pritchard (BP) has only advised his Chairman on a hypothetical basis and had not seen any of the documents that are relevant.

I was not persuaded by the BP arguments and I must confirm my earlier advice that the "corporate route" is not safe for HMG to adopt. In my view the only proper course is to negotiate for a sale under the terms of the UKCS agreements, with the object of getting all the necessary consents. Treasury Counsel and your lawyers agree.

I will enlarge on this at our meeting on 23 June and at the meeting of "E" Committee on 24 June but I thought it as well to give you advance notice of the position.

This is copied to the Prime Minister, all members of "E" Committee, the Financial Secretary (Treasury), the Lord Advocate and Sir John Hunt.

Yours ever,
Michael.

SECRET

23 JUL 1979

SECRET

18

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

PRIME MINISTER

BNOC : FUTURE STRUCTURE AND DISPOSAL OF ASSETS

In his minute of 18th July David Howell put forward a number of proposals on the related questions of disposal of BNOC assets and the future of BNOC itself.

2. I can understand David Howell's wish to clarify elements of UKCS policy and BNOC's future without damaging delay but I do not believe that we can make any sensible statement on the future of BNOC unless and until we have taken decisions on the question of disposal of BNOC assets. Any statement made before such decisions have been made would beg more questions than it answered. It is my intention to ensure that this afternoon's discussion at E(DL) puts us in a position to take decisions at next week's E Committee.

3. I share David Howell's view that BNOC's crude oil trading role should be retained together with its participation crude oil options because I believe they are vital to our security of supply, particularly since we are, through membership of the Community, prevented from interfering with exports of UKCS oil and because there are already indications that certain other major oil producing countries such as Kuwait, Nigeria and Iran are showing an increasing tendency to want to trade with state oil corporations rather than with multi-national oil companies.

4. I also agree that the confirmation of the Sixth Round Licences award should be announced as soon as possible so that UKCS momentum

is not lost. As David Howell says, the inclusion of BNOC's Sixth Round licences in any disposal of assets to BP would complicate matters considerably, and, moreover, as the Attorney General pointed out in his letter of 10th July would also have legal difficulties. In any event, I have doubts whether BNOC's licences should be vested in one company. Would this not further aggravate the already difficult situation on depressed exploration activity? Cannot the Sixth Round be announced with BNOC as partners and, if decisions are subsequently taken to dispose of their Sixth Round licence interest, these could presumably be disposed of by an open licensing round giving their Sixth Round partners first refusal. I very much doubt whether BNOC's Sixth Round interests should form any part of a sale to BP.

5. However, I see a number of difficulties with the other main proposals. I have real doubts about whether the setting up of an upstream subsidiary for BNOC's assets is a necessary first step to either a total takeover by BP or any lesser disposal of their assets. I shall be exploring the legal doubts about this route this afternoon with the Attorney General but from my point of view this route would not reduce the PSBR unless BNOC control of the subsidiary was given up entirely. Moreover, setting up one subsidiary would not facilitate the selling off of BNOC's assets piecemeal: indeed it would effectively foreclose this option.

6. I note that the proposal to dispense with BNOC's statutory advisory role will entail additional departmental manpower and related public expenditure. Whilst there is a possibility that the outcome of our considerations could be the retention of a substantial part of BNOC's upstream interests, it would not seem sensible to cut ourselves off from BNOC's advice, particularly since such advice would be based on first-hand experience of UKCS activities.

7. I also note that David Howell wishes to point up the possibility of a Seventh Round of licensing. I think this is something that we should look at separately outside these discussions in E(DL) once David Howell has put forward his proposed minute on the subject.

8. I am copying this minute to members of E and E(DL) and to Sir John Hunt.

(G.H.)

19 July, 1979

SECRET

17

ROYAL COURTS OF JUSTICE
LONDON, WC2A 2LL

01-405 7641 Extn 3201

July 1979

Nigel Lawson Esq MP
Financial Secretary
HM Treasury
Parliament Street
LONDON S W 1

Dear Nigel,

DISPOSAL OF PUBLIC SECTOR ASSETS

I have seen your letters of 16 July to Keith Joseph and Peter Walker about certain proposals to sell public sector assets in their spheres of responsibility. I think some further comment is called for from me before the next meeting of E(DL) on 19 July.

Industry Bill

2. I agree that legislation would be required to permit the sale of the Government's stake in the Radio Chemical Centre and Cable and Wireless.

3. As to the sale of assets of the British Steel Corporation, my letters to Keith Joseph of 10 and 16 July, and the Lord Advocate's of 12 July, are relevant. I now take you as saying that the BSC Board may not be willing to sell the assets under section 3(5) of the 1975 Act, despite the special provision in section 2(5)(b).

4. In this event the question will arise as to whether the existing powers of direction in section 4 of the 1975 Act are adequate to force a sale. I have no doubt that a direction to sell particular assets would be a direction of a specific character and hence that the power in section 4(1), which is limited to general directions, would be of no avail. Nor in my view is the limited power to give specific directions, in section 4(2), likely to be apt, although this would depend on the nature of the assets as to which I have too few details to advise with certainty.

5. Apart from sections 4(1) and 4(2), section 4(5)(a) in effect creates a prohibition on the forced sale of any iron and steel assets in Great Britain; thus the power is, on the face of it, inadequate to direct a sale of any assets in this category. Then the proviso in section 4(6) creates a further

/obstacle

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LONDON, WC2A 2LL

01-405 7641 Extn

obstacle in that no direction can be issued under section 4(5) if it prejudices the proper discharge of the BSC's statutory duties; this is a provision that would certainly be prayed in aid by anyone hostile to a forced sale.

6. On the wording of section 4 of the 1975 Act, and without resorting to the general principles set out in my letter of 8 June to David Howell, it seems to me that the powers of direction in that section are not apt to force a sale of the assets in question and that legislation would be required to enable this to go forward safely.

Market Towers

7. You have now given further details which lead to the conclusion that the CGMA could sell Market Towers under section 18(2) of the 1961 Act; from what you say it appears that the criteria for the use of section 18(2) are met, in that the building is not "required for the proper exercise or performance of /the CGMA's/ functions" and in that a disposal of it would be "calculated to facilitate the proper discharge of /the CGMA's/ duties ... or is incidental or conducive thereto". It is, of course, a requirement of section 18(2) that the CGMA should be of opinion that this is so, but again it appears from what you say that although the CGMA may initially be unwilling to confirm this, it would be unreasonable on the facts for them not to be of this opinion, and they may eventually be persuaded to sell using the section 18(2) power.

8. On this basis, and bearing in mind the objects of the sale as you describe them, I think it would be quite proper of Peter Walker to seek to persuade the CGMA to sell under section 18(2). If this fails, the power of direction under section 2(1) of the 1977 Act could naturally be considered but I will advise separately on this if it becomes a real issue. At this stage I only point out that section 2(1) requires prior consultation with the CGMA, and due weight would have to be given to any representations made by the CGMA which were inconsistent with what you say in your letter.

Forestry Commission

9. The sale of land in use or meant for use by the Forestry Commission is a matter on which I have not advised thus far

/and

ROYAL COURTS OF JUSTICE
LONDON, WC2A 2LL

01-405 7641 Extn

and at this stage, since there are no definite proposals and I have little information, I merely wish to put up a marker.

10. I understand that much of the land in question was acquired under section 39(1) of the Forestry Act 1967 by successive Ministers of Agriculture and has been placed at the disposal of the Commissioners, also under section 39(1); in the case of land acquired by Ministers before the commencement of the 1967 Act, or placed at the disposal of the Commissioners before that date, the provisions of section 39 apply equally by virtue of paragraphs 4(1) and 4(2) in Schedule 6 to the 1967 Act.

11. There is a statutory power for the Minister to dispose of land so acquired, in section 39(2) of the 1967 Act. The criteria that have to be satisfied before a sale can be effected are different in the case of Scotland than in the rest of Great Britain; in the former case the Minister has to be satisfied that the sale is desirable in the interests of rational land management, and would facilitate the discharge by the Commissioners of any of their functions, and in the latter case the Minister must be of opinion that the land is not needed, or ought not to be used, for the purpose of afforestation or any purpose connected with forestry.

12. I think it must be doubtful in present circumstances whether a substantial sale of land - much of which may not be suitable for development except as afforested land - could be brought within the terms of section 39 of the 1967 Act, although the difficulties may be less in the case of genuine "surplus" land than in the case of plantable reserve. The general principles stated in my letter of 8 June to David Howell are, for the most part, also relevant. Therefore at this stage I wish to enter a caveat and to suggest that legislation might also be required to authorise these sales. If a decision is taken to sell, I should wish to be consulted with full details of the assets in question so that I can give a more considered view.

13. I should also mention that the Minister of Agriculture has a limited power of disposal of land belonging to him in England and Wales, under section 90 of the Agriculture Act 1947; but on the facts available to me that power seems even less apt for the present purpose than section 39(2) of the 1967 Act.

14. This is copied to those who received any of your three letters of 16 July. I thought it appropriate to write direct

/to

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LONDON, WC2A 2LL

01-405 7641 Extn

to you, and I hope Keith Joseph and Peter Walker will forgive me for not writing to them personally.

Yours ever.

Michael

19 JUL 1979

SECRET

16

Treasury Chambers, Parliament Street, SW1P 3AG

19 July 1979

The Rt Hon David Howell MP
Secretary of State for Energy
Department of Energy
Thames House South
Millbank
LONDON
SW1

D 24/7

BNOC REVIEW

I have seen a copy of the Attorney General's letter to you of 10 July amplifying the views he expressed at E(DL) on 5 July, on BNOC's "carried interest" arrangements and disengagement from its equity interest in Sixth Round licenced areas.

In paragraph 3(i) of his letter the Attorney General raises points about public expenditure implications. I am not sure that the first point he raises would in fact have public expenditure implications if, as you propose in Annex 2 of E(DL)(79)6 BNOC simply gives up completely its interests in "carried interest" licences. However, there is another public expenditure point which I would like taken on board. "Carried interest" provisions do save public expenditure; they avoid expenditure on abortive exploration and postpone public expenditure on successful exploration. In view of this, when decisions are taken about BNOC's future I hope you will bear in mind that if the preferred solution entails BNOC retaining part of its exploration interests there are good public expenditure grounds for ensuring that the licences retained include those which have a "carried interest" provision. This would also help avoid the other problems raised by the Attorney General in his letter.

Copies of this letter go to the Prime Minister, members of E(DL), the Lord Privy Seal, the Secretary of State for Scotland, the Lord Advocate and Sir John Hunt.

NIGEL LAWSON

SECRET

19 JUL 1979

COPY N° 1 OF 23 COPIES

2 15

Prime Minister - To note

Then proposals were discussed in E(DL) today. They will come back to E next week. The Chancellor (Flag A) has serious doubts.

~~Prime Minister~~

~~Are you content with Mr. Howell's proposals to X & Y?~~

Dfy Clerk 19/7

SECRET

PRIME MINISTER

19/7

BNOC: FUTURE STRUCTURE AND DISPOSAL OF ASSETS

Following our discussion at E Committee yesterday, we are again going to return at E(DL) tomorrow to the difficult BNOC issue, and in particular to the two questions of disposal of assets to meet the Chancellor's target for realisations in 1979/80 and the future structure of BNOC itself. I shall of course be reporting to E(DL) my proposals for resolving these problems, having regard to yesterday's discussion, but I thought you should know how I believe we could proceed in a way which reconciles our various common- and absolutely vital-objectives.

First I think that we can agree that whichever way we go a first step has to be to form an upstream subsidiary in which the assets of BNOC are vested. This is a vital preliminary step either to a total BP take-over or to any lesser strategy for keeping assets in British hands. Could I therefore suggest that we take this step now? It closes no options: indeed, it is an essential preliminary so that we can carry out quickly any decisions which we reach later about the best way to meet the Chancellor's target.

Second, as far as BNOC's structure is concerned there seems to be a general acceptance that

a) at least for the time being the crude oil trading role should be retained, together with the participation options.

b) BNOC's statutory duty to advise should be abolished (so that there will therefore be an immediate need to strengthen the Department's internal specialist advisory team instead).

These are major steps and the quicker I can announce them the better the chances of avoiding serious dislocation in achieving our ultimate aims.

Third, the importance of confirming the first batch of 6th Round licences and pointing to the way to a seventh round, as soon as possible, has been recognised. Again the BP take-over possibility need not stop us doing this. I have spoken since yesterday to Sir David Steel and he agrees that rather than transfer all BNOC 6th round license interest to BP, which would be prolonged and tricky (even by the take-over route) we could deal with them case by case in a way which should satisfy the other licensees and does not delay our major purposes.

On this basis, therefore, it would be possible to proceed forthwith to a statement. This course would then enable us

(i) to announce the outcome of the BNOC review and the directions we want to go;

(ii) to let all the licence arrangements go forward;

(iii) to keep the way fully open for detailed discussions as to how much we sell off;

(iv) to give BP full time to prepare a properly organised take-over without an intervening hiatus; if that were the decision;

(v) to give ourselves full and adequate time finally to work out and overcome possible legal snags which at present seem to block a more precipitate announcement.

Subject therefore to the discussion in E(DL) tomorrow I would like to recommend this approach to E Committee together with a draft statement to Parliament which I would aim to make on Thursday 26 July. If this is accepted then I would have to inform Lord Kearton and the members of the Corporation immediately in advance, of the content of the statement and an indication of the options we are considering

for the upstream operation, though of course not mentioning the BP proposition. It is probable that he at least will wish to resign - he has as you know stayed on at my request beyond the 30 June, the date he suggested for his departure. I am therefore considering possible candidates for the job of caretaker Chairman until such time as the future disposal strategy, and role for BNOC's upstream side, is settled.

I have it in mind at the same time to make a statement about my plans for a further round of licensing (7th round), about which I will be minuting you separately.

CONCLUSION

The approach which I suggest here makes it possible to clarify at least some of the important elements of North Sea oil policy and the BNOC problem without further damaging delay, while leaving open for further consideration the best method of meeting the Chancellor's objective of raising substantial sums by means of disposals and doing so with minimum disruption to our overall policy. I believe a statement on these lines will be seen as consistent with a proper and orderly conduct of our oil policy, while not prejudicing in any way future decisions on disposals, and will ensure that the Government's standing and credibility on these issues is not diminished in a way which they would be if we deferred any statement, or reached hasty decisions now.

I am copying to Members of E and E(DL), and to Sir John Hunt.

D.H.

Secretary of State for Energy

18 July 1979

18 JUL 1979

SECRET

Energy No 14

10 DOWNING STREET

From the Private Secretary

18 July 1979

Future of BNOC

There was an error in my letter of 16 July recording the Prime Minister's discussion with your Secretary of State, the Chief Secretary and Sir David Steel. The last sentence of the second paragraph on page 2 of my letter should have read:

> "On the other hand, provided the Lords' decision on Burmah shares did not go against the Government, it would still have about 42% of the equity."

- not "26% of the equity".

I am sending copies of this letter to Alistair Pirie (Chief Secretary's Office), Martin Vile (Cabinet Office) and Bill Beckett (Attorney General's Office) who also has a copy of my earlier letter.

T. P. LANKESTER

W.J. Burroughs, Esq.,
Department of Energy.

SECRET

cc Mr. Wolfson

PRIME MINISTER

Future of BNOC

It was left at E Committee this morning that E(DL) Committee should look at the options for disposing of BNOC assets again on Thursday. But you also suggested that there might be a preliminary meeting of some of the key Ministers. I think you had in mind, in particular, that Mr. Nott should have his say.

Mr. Howell and Mr. Nott have this afternoon discussed this. They have agreed that a possible way forward would be for Mr. Howell to make a statement before the Recess which would say the following:

(i) BNOC is far too big and must be slimmed down at the very least.

(ii) All its upstream assets will be transferred to a subsidiary.

(iii) The sixth round licenses are confirmed.

(iv) The Government will consider urgently what assets should be sold off from the subsidiary.

This approach has the advantage of enabling Mr. Howell to say something about the future of BNOC and thereby ending the uncertainty; it means that the sixth round of licenses goes ahead and thus avoids the alleged disturbance of North Sea exploration; and it keeps all the options open on the sale of assets. Either the whole subsidiary could be sold off, which is of course BP's preferred option; alternatively, some of the subsidiary's assets could be sold; a further possibility is that the subsidiary could be "privatised" with shares being sold partly to private investors, partly to the oil companies, and some possibly retained by HMG.

This approach will not immediately meet the Chancellor's need because it does not spell out what assets will be sold. However

/ it is

it is worth considering. E(DL) will consider, and report back to you.

TL.

17 July 1979

10 DOWNING STREET

17/7/79

THE PRIME MINISTER

Tim.

I am very worried about the BNOC paper - it is the most one-sided I have ever seen. There is no attempt to give the other side - I will have a word about it with SNJ for Energy today.

The trouble is that the last Govt. [illegible]
merged cash limits & the Estimates.
There is in effect now no distinction
between the two in so far as
cash-limited expenditure is concerned.
This is why we are painted into
a corner over cash limits.

17/7/79

Don't forget BGC Wytch Farm
which is worth £100m.

Wytch Farm	£100m.
Viking	50
Strathspey	say 75
Ninian	400
	625

This leaves a much more manageable slice of BP to sell

360-450.

52

10%.

42%.

SECRET

2.9 13

Treasury Chambers, Parliament Street, SW1P 3AG

Copied from Econ Pol June 79
Disposal of fissile assets

Secretary of State
Department of Industry
Ashdown House
123 Victoria Street
LONDON
SW1E 6RB

16 July 1979

INDUSTRY BILL

In the light of the agreement of E (EA) on 11 July to your proposals on the future role of the NEB, preparations will be going forward for the drafting of the Industry Bill. This will provide, among other things, new powers to dispose of NEB assets. As I understand it, the intention is to introduce the Bill directly after the Recess so that it could receive royal assent by January at the latest. Obviously we do not want to jeopardise this timetable, but the Bill would provide an opportunity to seek powers to provide for certain other disposals on which we are relying to keep the PSBR in 1979-80 to £8¼ billion. Some of these possibilities have already been mentioned at E(DL) or in correspondence. But I think it would be useful to bring them all together so that we can clarify, in the context of the forthcoming E(DL) discussions, just what would be practicable and what our priorities should be.

E(DL) Committee have not yet reached final views on the disposal of BNOC and BGC assets, but subject to the Committee's decisions, I think that there is a good case for including in the Industry Bill provisions to give the Secretary of State power to dispose of BGC and BNOC oil field assets in any way he might think fit. Such powers would be useful for disposals next year even if not required this. I recognise that these powers could be included in the forthcoming Bill amending the Petroleum and Submarise Pipelines Act 1975, but this Bill could well not be enacted in time for disposal to be made this financial year.

It was also suggested at the last meeting of E(DL) Committee that we should investigate further the sale of 49 per cent of the Government's holding in The Radio Chemical Centre (TRC). I am sure that the TRC is a good candidate for disposal this financial year, but I see no reason why the Government should seek to retain any holding at all in the Company. However, I understand the sale of all the shares would require legislation and I therefore suggest that, subject to David Howell's views, the relevant provision, which would be very short, should be included in the forthcoming Industry Bill. Meanwhile preparations should be made for the sale of TRC so that the

proceeds could be received in time to be counted towards the £1bn total announced in the Budget.

As I said earlier, we clearly do not want to overload the Bill so as to jeopardise its timetable, but you might also like to consider, in the light of the Attorney's advice in his letter of 10 July, whether it should not also include a provision to make certain the powers to dispose of British Steel Corporation assets, and possibly also provide for the sale of Cable and Wireless. In the BSC case I understand that we need to be sure, at the least, that the Corporation can realise the specific assets shceduled for disposal during the current year without there being any need for the Board to confirm that the disposals are in the interests of the business.

The background to the present discussions of public expenditure in 1980-81 includes the assumption that we shall secure further receipts from asset disposals that will reduce public expenditure by £500 million in that year. The various possibilities are discussed in the paper I shall shortly be putting to E(DL). As well as selling shares in certain industries, we may have to look to nationalised industries to raise substantial amounts by disposing of further landholdings and possibly by selling self-contained operational units not integral to the main business. Since we may not be able to rely on the industries to cooperate voluntarily in making these further sales, we should perhaps consider also adding powers for the Government to enforce them to the various relevant programme Bills which will be going through Parliament during the current session. In the case of BSC, the Industry Bill might again be the vehicle; or alternatively the necessary provisions might be included in the Bill to denationalise shipbuilding and aerospace activities. In the case of British Rail, and perhaps also certain other surface transport nationalised industries, the forthcoming Transport Bill would provide the opportunity to secure the necessary powers (although, of course, I recognise that sales of business units are not Norman Fowler's preferred way of attracting private capital into this area, and that he would want if possible to avoid using such powers).

I should be glad to have urgent views on all this from you and your other colleagues concerned.

I am sending a copy of this letter to the Prime Minister, the Lord President, Members of E(DL) Committee, the Minister of Transport, the Attorney General and Sir John Hunt.

NIGEL LAWSON

10 DOWNING STREET

Prime Minister Yes JR.

The E discussion on BNOC will obviously merge into E (DL). It would be a good idea if Mr Lawson joined E for the BNOC item. Agree? (He is the only E (DL) member who is not a member of E).

JR. 16/7

Prime Minister.
Since receipt of this brief, we have also received a Paper from the Chancellor (Flag A)
JR Ibbs 4/7

CONFIDENTIAL

Ref. A09984

PRIME MINISTER

Future of BNOC

(E(79) 20, 21 and 22, also E(DL)(79) 6)

BACKGROUND

There was an inconclusive discussion of this range of subjects in E(DL) under your chairmanship on 5th July. You asked the Secretary of State to produce a further background about the case for retaining BNOC. It has turned out to be three papers, one of which is not self-contained but refers back to his earlier ones. The presentation is confused, and the papers have been circulated late. You would be justified in complaining on both scores. You have since agreed that the strategic issues should be considered in E, followed immediately by discussion in E(DL), again under your chairmanship, of the disposals. In practice, the two discussions will tend to telescope, and the E discussion is in any case likely to run late. At some point you may therefore want to bring in the Financial Secretary who will be waiting around for E(DL). This one brief is intended as a guide for both meetings.

2. There are three important timetable constraints:

(i) Mr. Howell wants to make a statement about the future of BNOC and about the confirmation of awards under the 6th licensing round before the Recess. The case for an early announcement on the future of BNOC is deployed in E(79) 22. The complication arising from the 6th round is explained in paragraphs 6-8 of E(79) 21. Both, if accepted, point to the need to reach decisions at this meeting. (Though you may feel that, at least an announcement on the future role of BNOC could wait till after the Recess).

(ii) The Financial Secretary wants to make a statement on disposals before the Recess. Now that the Government has forgone the option of an early move on the BP shares, this may be less essential, and I think you should question him on the operational necessity. The Treasury has got through the Finance Bill debates without being pressed for a statement of its intentions on disposals, and market rumours have died down.

(iii) There may be a need for legislation to give effect to these decisions. The first part - to allow BNOC to make limited disposals in this financial year - is urgent, but could probably be tacked on to the Industry Bill. The second part, to restructure BNOC and allow for private capital, is not essential to make up the 1979-80 disposals package, and will have to come later. Nevertheless, policy decisions today will allow a lot of drafting to proceed.

3. In his main paper, E(79) 22, the Secretary of State for Energy proposes a holding operation at this stage:

(a) Disposals of £200 million worth of assets now, including Viking and Statfjord, subject to the legislation point above.

(b) A move towards further disposals and/or privatisation, but in a longer timescale.

4. However, colleagues may feel that this does not go far enough. In particular, it would not provide anything like the total Energy contribution to the Chancellor's £1,000 million this year if the BP shares are not sold. The discussion will therefore have to go wider than Mr. Howell's immediate proposals.

5. The decisions which you will need at this meeting are therefore:

(a) On the future role of BNOC: including its upstream activities, its involvement in oil trading and its advisory role.

(b) If BNOC is to be run down, the destination of its assets, and of methods of involving private capital.

(c) If £200 million worth of assets is not good enough this year, then what other options to pursue: BP shares; further short-term disposals of BNOC assets, including perhaps Ninian; or the larger transfer of BNOC upstream interests to BP.

The first of these questions is really one for E; the other two spill over into E(DL).

HANDLING

6. I suggest you concentrate discussion on the three issues, making this clear from the start.

(a) The future role of BNOC.

(i) Upstream activities: The Committee might look first at the 'note by officials' circulated with E(79) 20. The Secretary of State, in his covering note, appears to distance himself a little from this paper. The key figures are in Annex 1. Taking royalty oil in kind gives us 12 per cent of United Kingdom Continental Shelf oil under Government control. BNOC equity oil gives us another 6 per cent, or 18 per cent in all. The smaller United Kingdom companies give us a further 8 per cent but we cannot control this so directly. Shell and BP have another 25 per cent but Mr. Howell in the paper has lumped them with other multinations because they behave in the same way, rather than as "United Kingdom" firms. The present participation arrangements allow BNOC to control roughly an additional 20 per cent of North Sea production at its discretion and give potential control of yet a further 20 per cent if the sale back clauses of participation agreements are operated. Thus at the maximum BNOC/BGC can control up to 55 per cent of North Sea output, of which about two-thirds would be participation oil. Of course the participation oil has far more strings attached to it than has equity or royalty oil. And the equity oil is the most immediately usable. It derives entirely from BNOC's direct involvement in fields. The Annex to E(79) 21 shows that BNOC has equity access to about 125 million tons of recoverable reserves, of which 15 is in Statfjord and 34 in Ninian. Ninian is already on stream, and Statfjord starts next year.

(ii) Trading. The figures in the Annex to E(79) 21 show that BNOC derives control of between 19 and 37 per cent of United Kingdom production from its participation agreements (depending on the use made of sale-back clauses). Mr. Howell recommended (paragraph 12 of E(DL)(79) 6) that the BNOC should retain these participation rights. Since they require BNOC to purchase oil

at market price, these rights have, theoretically, no cash value. Obviously the companies would prefer to have unfettered control over this volume of oil, but they do not seem prepared to pay a price to buy these rights back (any more than BNOC paid for the right in the first place). To retain the 'participation rights' does not, therefore, cut across the Chancellor's strategy. The participation agreements were attacked by the Government in Opposition, and might theoretically be challenged in the European Court. But there is likely to be agreement that the Government should hold on to these rights. That in turn means keeping BNOC in existence as a vehicle to exercise them: they could not be handed over to BP, and are not easily exerciseable by Government direct. You might seek to establish quickly whether the Committee agrees with this view. If so it will simplify the rest of the discussion.

(iii) BNOC's Advisory role. Mr. Howell proposes (paragraph 22 of E(DL)(79) 6) to abandon the statutory advisory role of the BNOC while still looking to them for advice as appropriate. But this done the key question is whether the BNOC should retain its present membership of the operating Committees for each field where it has not got an equity interest. The argument for retention is that this gives information about costs, to lesser extent about prices and about reservoir engineering, likely reserves, flaring and so on. Of these, the one with most cash value is information about costs and pricing. Inland Revenue have other means of obtaining this information, although the BNOC material is probably a useful supplement. The other information can, theoretically, be obtained directly by the Department of Energy: though once again BNOC's direct involvement gives it an alternative source. Mr. Howell said last time that he receives conflicting advice on the value of the information and advice he gets from BNOC. But although it is a source of friction with the oil companies, the advisory role will continue informally even under

Mr. Howell's proposal to abolish its statutory basis. The real merit and value of BNOC's membership of operating committees (except where it is an equity partner), is a matter on which the Committee will wish to look to Mr. Howell for technical advice. BNOC could, of course, continue as a trading organisation without such membership.

(b) How can private capital be introduced into BNOC, and to what extent should its assets be run down? At this point this discussion shades off into E(DL) territory and you might bring in the Financial Secretary if you have not already done so. It was at this point that the discussions got into difficulty last time. Mr. Howell is afraid that large scale disposal at this stage will make BNOC a less attractive subject for privatisation. But the form of privatisation which he proposes would still leave BNOC in existence, with control over the oil. (See, particularly, paragraphs 20-21 of E(DL)(79) 6). This is an ingenious package, which would produce cash from the sale of minority interests in the new subsidiary company. It would also, apparently, avoid the 'pre-emption' problem which gives the other partners first refusal over any assets which BNOC sells: (see paragraph 9 of E(79) 21). It will leave BNOC in existence, as a trading organisation, though with progressively less equity oil. If the private interests were, for example, in a newly-established city consortium, control would remain in British hands, but this would not necessarily guarantee that the oil would flow to British use - particularly since the new owners would not have access to their own refinery capacity. The net result would still be some reduction in the Government's direct control over oil. For this reason, Ministers may be reluctant to pursue this option too far - though, since it is envisaged as a piecemeal disposal operation, the legislation could be introduced and interests in one or two fields disposed of experimentally.

7. If the decision is to run down BNOC, and to allow the introduction of some private capital, should the assets be retained in British hands, and if so how? The Committee should by now have agreed the participation rights themselves are

unmarketable. In that case, the choice lies between disposing of equity interests directly, or hiving them off into subsidiary companies, and disposing of shares in these subsidiaries. A secondary choice is whether to sell these interests to existing or newly formed British interests, or more widely: and, if the decision is to retain in British ownership, whether to dispose piecemeal, or attempt a block sale to BP. The new paper E(79) 21 deals with these options in detail. But you should ask the Secretary of State to supplement this by reporting orally on his discussion with Sir David Steel, particularly about the idea which the Secretary of State for Trade floated at the last meeting. (This was, briefly, for BP to finance the operation by raising a new loan, with equity rights attached. In order to preserve a 51 per cent interest in BP, Her Majesty's Government would have to be prepared to take up its share of this loan and attached rights, and this would reduce the net benefit of the sale to BP. But since the entire BNOC holding has a net present value estimated in Table 1 of E(79) 21 at between £795 million and £1232 million, the net benefit could still be very large, although it seems most unlikely that it could all be realised in 1979-80.).

/Note: the same table estimates the net revenue of the holdings to 1984 as £1400 million and the liability for extra capital in the same period as £685 million/.

8. The issues here become highly technical. The point to establish early on is whether, as appears to be the case, there is little prospect of pressing ahead with a block disposal to BP in 1979-80. If that is so (and it will disappoint the advocates of such a scheme, including the Financial Secretary) then the choice does come down once again to the sale of the BP shares this year versus a shortfall on the Chancellor's £1000 million target, or finding some other means of balancing the books. Looking further ahead if it is accepted that a block sale is impracticable this year but remains a long term option, there is no need to reach final decisions on this particular issue at this meeting: the issues can be remitted to another meeting of E(DL) under the Chancellor, before or even after the Recess. If, unexpectedly, it emerges that a block sale to BP could be completed in the current year, despite E(79) 21, then again you might seek to record agreement in principle, and once more remit the details to the Chancellor.

The Committee should however note that all of the options - hiving off, block sale and probably the limited disposal (say Statfjord and Ninian only) - would require legislation.

CONCLUSIONS

9. I think you might try to set out conclusions on the pattern as suggested above; there would be four. The first three might be recorded as conclusions of E, and the last as a conclusion of E(DL).

10. Subject to the course of discussion, these might be:

(i) That the Committee sees a continuing role for BNOC, as a trading organisation, retaining its participation rights, but disposing of some /or all/ of its equity interests, and /probably/ deprived of its statutory advisory role.

(ii) That legislation should be prepared to provide for the introduction of private capital into BNOC (any remaining points of detail to be decided by E or (E(DL) after the Recess).

(iii) That the disposals of assets, whether to other oil companies or for the sale of equity in subsidiaries of BNOC, should be pursued only to the extent that it does not involve any significant loss of control over oil. /The Committee will need to decide whether sale to BP involves "loss of control" in this sense/.

(iv) Either that disposals in 1979-80 should be confined to the £200 million offered by the Secretary of State for Energy, and that he should pursue the details with the Financial Secretary urgently; or that he should aim to dispose of more in 1979-80 /including Ninian?/ and (in either case) that he should seek to attach additional clauses to the Industry Bill to facilitate these disposals; or alternatively that he should proceed urgently, in consultation with the Financial Secretary/Chancellor of the Exchequer, and with the Chairman of BP, to make arrangements for an immediate sale of most or all of BNOC's upstream assets to BP, to be financed by a loan issue and noting that Her Majesty's Government would take up its share of rights and retain control over BP. (If this is not the

decision, you will also need an additional conclusion: that the Committee should return to the question of selling BP shares after the Recess, on the basis of the original proposals put forward by the Financial Secretary in E(DL)(79) 5).

11. You might also note that there is another meeting of the Sub-Committee on Thursday under the Chancellor to take a paper on longer-term disposals; on disposal of land; on British Aerospace; and - if necessary - on British Airways /on which the Secretary of State for Trade hopes to make a statement on Friday/.

for (John Hunt)

16th July, 1979

SECRET

12

10 DOWNING STREET

From the Private Secretary

16 July 1979

Dear Bill.

Future of BNOC

The Prime Minister held a meeting this afternoon with your Secretary of State, the Chief Secretary, and Sir David Steel and Mr. Adams of BP to discuss the future of BNOC. The following are the main points which came up in discussion.

The Prime Minister explained that the Government needed to raise substantial sums through the sale of assets during the current financial year. The earlier intention had been to rely mainly on the sale of BP shares with a contribution from the sale of BNOC assets amounting to £150m - £200m. However, there would be advantage in raising considerably larger sums by selling off BNOC assets and retaining the Government's shares in BP in tact. There was no case for continuing to have a state-owned oil company, and she understood that BP were attracted by the idea of purchasing all of BNOC's assets. There was the separate question of BNOC's access to North Sea Oil through the participation agreements. Her own view was that these rights could be dispensed with without affecting the UK's security of supply. Other countries, such as the US, appeared to be able to insist on the private oil companies disposing of their oil domestically without a Government controlled intermediary such as BNOC; and in recent months, the participation agreements did not appear to have improved our position.

Mr. Howell said that various options had been explored with BP, but their preference was to purchase all of BNOC's production and exploration properties, including those allocated to BNOC in the 6th Round. However, there were considerable difficulties in this approach. These were set out in paragraph 5 of his briefing minute. It would take time to overcome them. In particular, any unilateral attempt to transfer BNOC's rights in the 6th Round to BP could well lead to litigation; and the transfer of other assets could require protracted negotiation. One way of dealing with the latter would be for BNOC to transfer its assets to a subsidiary whose shares would then be acquired by BP. This was the route favoured by BP. If the Government and BP were to go along this route, both sides would have to be firmly committed in principle before announcing anything. It would

/be

SECRET

be important that BP should be in a position to take over the management of BNOC's operations as soon as the announcement had been made; otherwise, there would be a damaging hiatus. He had hoped to make a statement about the future of BNOC before the Recess, and also to announce the confirmation of the 6th Round Licences. It seemed unlikely that this would be possible if it were decided to pursue the BP takeover of BNOC.

Sir David Steel confirmed that BP's preference would be to purchase all of BNOC's production and exploration properties, and in order to avoid having to negotiate with BNOC's partners they strongly favoured the transfer of BNOC's assets to a subsidiary which BP would then purchase. If this were done, they thought the problems mentioned by Mr. Howell were far from insuperable. Even the difficulty of the 6th Round Licences could be exaggerated: these Licences had not yet been issued, and therefore the prospects of the companies securing substantial damages from the Government in litigation were small. It ought to be possible to arrive at Heads of Agreement by the end of the financial year, which would allow an advance payment from BP for the purchase. Based on past experience with other purchases of North Seal assets it should not be too difficult to reach agreement on the valuation of BNOC's assets - though they appreciated that this particular valuation would come under much greater scrutiny than usual. There was, however, the problem of financing the deal. A Rights Issue amounting to about £750m would be necessary. The Government could either take up its share, but this would reduce the net proceeds from the deal; alternatively, it could forego its share of the Issue, but this would mean reducing the Government's equity stake in BP. On the other hand, provided the Lords' decision on Burma shares did not go against the Government, it would still have about 26% of the equity.

Sir David went on to say that, nonetheless, he was concerned about the political repercussions of BP taking over all of BNOC's assets. This might lead to demands that the Government should have a closer control over BP's activities. Before embarking on the purchase, BP would want the Government to re-affirm its traditional non-interference in BP's affairs. In addition, he felt that the retention of the participation agreements by a BNOC limited to trading in oil would avoid much of the political pressure. In any case, although BP had been opposed to these agreements initially, they now felt that there was advantage for the nation in their continuing. The Chief Secretary added that both on merits and for political reasons it would be very unwise for the Government to renounce the agreements. Moreover, as Sir David Steel had suggested, it would be easier to maintain the Government's arm's length relationship with BP if they continued.

Summing/

Summing up, the Prime Minister said, subject to discussion by Ministers the following day, she would like BP's favoured option to be explored further. It would be important to establish very quickly the timetable of events, if this course were to be pursued - taking into account Mr. Howell's desire if possible to make announcements before the Recess on the future of BNOC and on the 6th Round Licences.

I am sending copies of this letter to Alistair Pirie (Chief Secretary's Office) and to Martin Vile (Cabinet Office).

Yours ever,

Tim Lankester.

Bill Burroughs, Esq.,
Department of Energy.

COVERING SECRET

Reference 11

Duty Clerk
10 Downing Street

Enclosed is the minute promised from my Secretary of State to the Prime Minister, as briefing for her meeting with Sir David Steel. I should be grateful if you could add a copy of E(DL)(79)6 to the background papers already attached.

John Arnott

John Arnott
APS/Secretary of State for Energy
Room 1237
Thames House South
Tel No. 211 7214

14 July 1979

CODE 18 - 78

SECRET

PRIME MINISTER

Introduction

You are meeting Sir David Steel on 16 July with the Chief Secretary and myself. I was asked at E(DL)3rd meeting to explore with Sir David Steel his reaction to a number of options whereby BP might take an interest in or take over BNOC's upstream assets. I have had two meetings with Sir David, and attach a copy of the note which he prepared as the basis for our second discussion. You will want this.

2 I am also attaching by way of background the papers on the future strategy for BNOC which I have circulated to colleagues for discussion at E Committee on 17 July. The two points I would like to emphasise as background to our discussion with Sir David Steel, which are covered in these papers are:

(i) the essential contribution that a state oil trading operation with access to the oil available under participation agreements can make to securing our oil supplies;

(ii) the options for BNOC's upstream operation which range from a preliminary slimming down, prior to introduction of private capital, to outright disposal of all its upstream assets.

3 The options which are covered by Sir David Steel in his note show ways in which BP might help us in meeting our objectives for

/BNOC's

BNOC's upstream side with minimum disposal to foreign owners depending on the policy decisions which may be taken about BNOC's future.

BP's views

4 As you will see BP's clear preference is for outright acquisition by BP of all of BNOC's upstream assets, and it is the implications and feasibility of this approach that the note concentrates on, and which I have developed in my discussions with him. I have not thought it necessary at this stage to probe closely BP's reasons for preferring this option, nor the implications of the other options, although if in subsequent consideration of the matter with colleagues we come to the view that the outright disposal of all BNOC's assets to BP is unacceptable, then we are still at liberty to pursue the other options with BP, and Sir David has expressed himself ready to do so at any time.

5 I think we should be quite clear that if BP's preferred solution were to be accepted as being consistent with the future role which we envisage for BNOC, its execution would be a very high risk course, and would give rise to a number of difficult problems. You may wish therefore to concentrate discussion with Sir David on the problems that might arise from his preferred option, and I note these below together with my comments in the light of my discussions with him:

a) Price: Negotiation of an agreed price is accepted by BP as likely to take time - in BP's view hanging mainly on our respective views of future oil prices. BP suggested this might take 2-3 months. This may be a

/serious

serious under-estimate; the oil price is only one of a number of important parameters that will have to be considered including estimates of recoverable reserves, production profiles and BP's tax position. (There is no point in getting a good price out of BP if the Inland Revenue simply foots the bill). It is essential that we should be able to demonstrate publicly that we have realised the full value of BNOC interests, and that BP have not got anything on the cheap. It is equally important that BP accept that their interests too would not be served by an apparently very favourable deal, since this could expose them to future political pressures.

b) HMG's relationship with BP: BP would want the Government's traditional non-interference in BP's commercial affairs to be reaffirmed. With such a large stake in the UKCS accruing to BP (including BNOC's interest approaching 22% of reserves and 24% of licensed territory) I doubt whether in practice the sort of arms length relationship that BP has sought to maintain could or should be continued at least in respect of UK oil operations.

c) Partner pre-emption rights: BP accept that if assets are transferred to BP by the assignment route, BNOC's partners rights of first refusal could make for extremely protracted negotiations lasting as much as a year. BP suggest that the assets are vested in a BNOC subsidiary whose shares are then acquired by BP. This certainly

/disposes

disposes of the pre-emption rights, but such a move should expose HMG to criticism that we had used a transparent device to circumvent the contractual rights of BNOC's partners.

d) 6th Round Licences: None of these licences has yet been confirmed. BP's view was that partners would welcome BP instead of BNOC (this may well not be true of small companies in particular). Nonetheless BP would not wish to take on the benefit of the various carried interest provisions which applicants had offered BNOC. I remain dubious about pressing ahead with transferring these licences to BP on the grounds that the substitution of BP for BNOC in the licences almost simultaneously with their issue, could be regarded as invalidating the licences. I think we would have to seek the specific agreement of BNOC's partners case by case.

e) BNOC staff: BP confirmed that it saw no problem in absorbing management all the way to heads of operational divisions and would say so at the start. The top management would be more problematical. BP accepted that the period of uncertainty between announcement of the plan and completion should be kept to a minimum and that we should try to settle the main lines of the deal before announcement. This would probably mean deferring an announcement until October (which would also mean deferring an announcement about our plans for future licensing, with a further risk to North Sea momentum.)

/f) Finance:

(f) Finance: BP's preference is for a rights issue to raise the bulk of the necessary finance; this would involve us in either reducing our holding in BP, or using a major part of the proceeds of sale of assets to take up our rights. Whatever financing package emerged BP think a rights issue raising a minimum of £500 m would be needed.

(g) Timing and Legislation: BP would be willing to start work on detailed negotiations as soon as HMG had declared its intentions. Any deal would have to be conditional on the passage of the necessary legislation. This would need to be introduced as soon as Parliament reassembles. If BP's suggestion for avoiding pre-emption right difficulties ((c) above) is adopted then BP think there should be no problem in securing proceeds of sale by end March 1980. If not there would have to be a large payment in advance.

6 You may wish to probe BP on all these points. I should add that while BP may consider that from its point of view there should be no difficulty in disposing of all the problems outlined above within the timescale envisaged, the same problems may prove much more difficult for us to overcome from our side, especially where solutions may be politically sensitive. In this context I am ... attaching a note prepared by my officials which examines the problems

that we will have to overcome. Perhaps none of these problems is insurmountable. But there is a serious risk of chaos if anything goes wrong.

7 A copy of this note goes to the Chief Secretary.

D.H.

SECRETARY OF STATE FOR ENERGY
3 July 1979

Top Copy : Econ Sit, May 79
Domestic Monetary Policy

cc Mr. Whitmore
Energy - BNOC

NOTE OF A MEETING BETWEEN THE PRIME MINISTER AND THE GOVERNOR OF THE BANK OF ENGLAND ON FRIDAY 13 JULY 1979 AT 1630 HOURS

The following are the main points which came up when the Governor called on the Prime Minister:

I. EMS

The Prime Minister commented that, had the UK joined the Exchange Rate Regime, we would have been forced to change sterling parity in relation to the grid. The Governor said that this was not necessarily the case. There would certainly have been upward pressure against sterling's maximum limit; on the other hand, this pressure might have been limited to some extent by the fact that market operators would have thought it unlikely that sterling's parity would have moved so soon. On the other hand he thought that against the current background of turbulence in the exchange markets, which was likely to continue for a while, it was best that the UK had not joined the Regime.

II. June Banking Figures

The Prime Minister commented that the June figures were even worse than the Governor had predicted at the meeting on the mortgage rate the previous week. The Governor said that this was so - including the "acceptance leak", lending to the private sector had been £1,250 million against £1,200 million which he had forecast. The high figure seemed to be due primarily to the June spending spree, which was now reflected in the provisional retail figures. The Prime Minister said that she continued to be concerned about the stock relief provisions, which tended to exaggerate the need for working capital since there was an incentive for businesses to build up their industries; she was also concerned about the tax provisions on leasing which also stimulated bank lending. The Governor replied that the leasing provisions did encourage investment; however, he understood that the Inland Revenue were looking at them.

III. Interest Rates

The Prime Minister said that she was worried at the prospect of interest rates having to stay high, though she fully accepted that - while the banking figures continued bad - there was no alternative. The Governor commented that the future level of

/ interest rates

interest rates depended very much on what happened to wages. If wage inflation accelerated, interest rates would inevitably stay high. In addition, interest rates in other countries were moving up. The Germans had just announced a 1% increase in their discount rate, even though Dr. Emminger had been implored - at the recent Central Bankers meeting in Basle - to avoid this. The Dutch and the Belgians had been obliged to follow. The Germans were clearly trying to fight inflation by keeping the DM up.

IV. The U.S.

The Governor said that the US economy was almost bound to go into recession after four years of rapid growth and with inflation slowing the economy down. Inflation over the last six months was running at an annual rate of 14% - this was partly due to the oil price increase, but food prices were also rising rapidly partly because of fears about the Russian harvest. It was uncertain what the Administration would do. With the election coming up, they would be under pressure to reflate and relax interest rates. But if they did, the dollar would certainly slide.

V. Gilts

The Governor said that the authorities had sold sufficient gilts to cover the Government's financing needs up to the end of August; but it would be important to make further substantial sales so as to bring in funds in September. A new short tap was being issue that day; it would be for decision the following week whether a new long tap should be issued.

VI. Sale of BP Shares

The Prime Minister said that she had stopped the sale of the BP shares in July. The alternative options needed to be considered more carefully, and in any case a sale later in the year might well produce larger proceeds. She had also been concerned that the Treasury were pressing to sell in New York and Frankfurt as well as in London. For political reasons, even though foreigners might buy in the secondary market, it was important to limit the sale to London. One further consideration was that the Lords' decision on Burmah might go against the Government. (The Governor commented that a final decision on Burmah could not be expected until October 1980.) One alternative to selling off BP shares was for

BNOC's assets to be sold virtually in their entirety. This was being considered. Asked whether the sale of BP shares to the institutions would be additional to their purchase of gilts, the Governor replied that there would be some substitution, but on the whole, purchases should be additional.

R.

16 July 1979

ACTION

SECRET

E(79)22

NOTE

In view of the exceptional commercial sensitivity of some of the matters referred to in this memorandum, recipients are asked to ensure that its confidentiality is strictly observed.

SECRET

ACTION

SECRET

E(79)21

NOTE

In view of the exceptional commercial sensitivity of some of the matters referred to in this memorandum, recipients are asked to ensure that its confidentiality is strictly observed.

SECRET

Copy No 1 of 5 copies of Copy No 1

SECRET

8

Prime Minister

This is David Steel's paper.

Copy No. 1

~~24~~ ~~26~~ A

BP'S RESPONSE TO CERTAIN PROPOSALS ON THE NORTH SEA

HMG has invited BP to consider certain proposals against the possibility that HMG might prefer to raise up to £1000 million by means other than selling a substantial part of their shares in BP, whilst at the same time reducing BNOC's activities to those of a State oil trading company.

The following proposals have been put forward for consideration:

a) Purchase outright some of the assets of BNOC for cash e.g. their interests in Viking, Statfjord, Thistle, Ninian.

b) Purchase all BNOC's production and exploration properties (including those allocated to BNOC in the Sixth Round), and also the oil producing properties of BGC, with due consideration for the position of staff, to be financed possibly by loan stock with warrants. Part of the consideration would be the taking over of the loan liabilities of BNOC.

c) Purchase a minority holding in a new upstream subsidiary of BNOC in which BNOC would retain 51%, and the other 49% could be shared with other UK oil companies and private investors, with BP having rights to up to 49% of the oil.

d) Some combination of (a) and (c).

Under all proposals, HMG would retain a right of "participation" i.e. a right to purchase 51% of the total oil produced which it would be prepared to sell back to the owning company at the same price, subject to Government stipulations on destination and contract terms.

BP's Views

Proposal (a) would in our judgement not justify incurring the serious political hostility and exposing BP to becoming a political football, for the sake of only a partial solution to the problem. It would also involve negotiations on the value of each field which at best could cause serious delays.

/...

Proposal (c) would involve BP investing considerable sums in a company whose operations, future development expenditure and crude disposal it would not be entitled to control, to whose cash flow it would not have access, and which could find itself in a situation of conflict of interest with any other oil company participant and indeed with BP's own wholly-owned exploration company.

Proposal (d) - some combination of (a) and (c) might be worth considering provided other oil companies were not involved and provided BP became the operator of the company to be established under (c).

Proposal (b) appears to be the clearest solution and to be compatible with BP's commercial interests. The initial reaction of the BP management is to pursue this proposal, subject to certain assurances and subject to the views of the full BP Board which will be necessary when a firmer proposal has been evolved.

Operational Aspects

A take-over by BP at a single price of the whole of BNOC's assets would avoid some of the difficulties of valuing individual holdings in a variety of fields. Moreover, it is the solution which would clear up the confusion which exists overseas between BP and BNOC and which would be more acceptable to the international companies than any partial solution which left BNOC an operating role. Foreign companies could be expected to accept BP's replacing BNOC in equity interests and operatorships, but for BP to assume the position preferentially awarded to BNOC in Sixth Round licences of a 51% interest carried by other companies through the exploration phase might raise problems. It should be possible to find solutions. Under any scheme the transfer to BP of BNOC's interest in licences in which it has partners may be difficult where those partners have pre-emptive rights. This will depend on the wording of individual agreements but we assume that HMG will be able to overcome such difficulties, for instance by putting the interests to be transferred into a limited company subsidiary of BNOC and then transferring that company to BP.

The operating staff of BNOC could be absorbed into BP's operating organisation. BP's management capability would be extended in running the combined exploration and production operation but we believe this could be done without undue strain.

Financial Aspects

Assuming for illustration that the BNOC properties had an agreed value of £1 billion, the purchase price plus future development expenditures could we believe be financed by the Group subject to the matters referred to below. The timing

/...

and method of financing would however be critical, because of the heavy initial outlay and the negative cash flow in the early years. BP could not meet the cash element of the purchase price and the assumption of the BNOC loan from its existing resources or cash flow. To meet it by loan financing would raise the Company's debt equity ratio to an unacceptably high level particularly bearing in mind the probability that OPEC as a whole will follow the example of Saudi Arabia and reduce credit from 60 to 30 days. This would result in difficulty in obtaining either the sums of money now required or future financing on reasonable terms. To use convertible stock or warrants would serve no purpose but would overhang the market for BP shares.

It would therefore be desirable for BP to raise the additional finance required for the purchase to the maximum extent by way of a Rights Issue, with the balance by way of a loan probably on the Euro-dollar bank market. We believe the market could support a Rights Issue of £750 million. To the extent that HMG took up all or part of their share of the Rights Issue, this would of course reduce their net receipt from the cash element of the sale of BNOC assets. Alternatively a scheme could be devised under which it would be open to HMG to reduce the call on them for cash by selling their rights, thus allowing their total shareholding in BP to fall somewhat below 51%.

Relationship with HMG

Whether HMG retains 51% of BP or less as a result of this exercise, it is of course well known that the powers of the Government Directors derive from the Articles of Association and not from a majority shareholding. It will therefore be essential that the traditional policy of non-interference in the Company's commercial affairs be reaffirmed in the clearest terms, so as to ensure the success of the financing itself and also to dispel any misapprehension at home or abroad as to BP's independence of management in respect of the properties acquired from BNOC, as well as the remainder of its business. The commercial interests of the Company will require the most careful consultation with HMG on the way in which the deal is to be presented and justified as being not only financially attractive, but also consistent with the national interest, so as to minimise the political risks to the increased BP interest in the UK.

Conclusion

In BP's view proposal (b) is the preferred solution of those indicated, however if it is concluded that none of these is feasible, the Company would be happy to discuss alternative suggestions or to revert to the idea of a major sale of BP shares.

12th July, 1979

SECRET

~~Econ Pol~~ 28

7

Lord Advocate's Chambers
Fielden House
10 Great College Street
London SW1P 3SL

0515
Telephone : Direct Line 01-212 0761
Switchboard 01-212 7676

Copied from Econ Pol June 1979
Disposal of Public Sector Assets

12 July 1979

The Rt Hon Sir Michael Havers QC, MP
Attorney General
Attorney General's Chambers
Royal Courts of Justice
Strand London WC2

12
1311

Dear Michael,

DISPOSAL OF PUBLIC ASSETS

I have seen your letters of 10th July 1979 to David Ennals and Peter Walker on the BNOC Review and Market Towers building respectively.

In the case of Market Towers I would agree that unless the Authority are satisfied as to the proviso in section 18(2) of the 1961 Act they would not be entitled to sell and consequently if the Authority were opposed to a sale it would be dangerous to make a direction under section 2(1) of the 1977 Act.

In respect of the BNOC situation although strictly speaking they are not legal points, I would agree with what you say in paragraph 3 (i) and (ii). Similarly I think the point you make in paragraph 3 (iii) is a valid one although obviously it is impossible to predict the effect of such a proposal.

I would also agree with the difficulties which you foresee in relation to the proposal that BNOC should relinquish its equity interests in sixth round licensed areas.

I am copying this letter to the Prime Minister and to the other recipients of yours.

Yours ever,

James.

MACKAY OF CLASHFERN

SECRET

Original: Cam PR (Council Hearst) May 79

PRIME MINISTER

MEETING WITH THE CHANCELLOR - THURSDAY, 12 JULY AT 0855

The Chancellor is coming to discuss his draft papers on the National Forum and the Economic Advisers' Council. These are attached. If you can reach agreement with the Chancellor on them, they could be put on the agenda for E Committee for next Tuesday. That meeting will be continuing the discussion on pay, and these papers would fit well with them.

The Chancellor is likely to raise two other points with you:

(i) Handling of the EMS review. Sir John Hunt's advice on this is at Flag A.

(ii) Your meeting with Sir David Steel next Monday. The Treasury have heard - not from us - that you are meeting Sir David along with Mr. Howell. The Chancellor would like a Treasury Minister to be present. This seems not unreasonable since the Treasury is responsible for BP: the Government's shares are vested in the Treasury Solicitor, and the Government directors are appointed by the Chancellor. The Chancellor himself will be in Brussels on Monday; presumably it would be for the Financial Secretary, who of course has been taking the lead on assets disposals, to attend. (For Monday's meeting, I am getting a brief from the Department of Energy, which will include a report from Mr. Howell on the meeting which he has already had with Sir David in accordance with the guidance given by E(DL) last week.)

11 July 1979

TL

The Chancellor has also sent a note (Flag B) on the international economic situation - which he may refer to.

SECRET

ROYAL COURTS OF JUSTICE
LONDON, WC2A 2LL

01-405 7641 Extn

10 July 1979

Dear David,

BNOC REVIEW

1. I am writing to amplify what I said on 5 July at E(DL) about the posposals for BNOC to negotiate out of the "carried interest" arrangements in the sixth licensing round and to disengage from its equity interests in sixth round licensed areas. These proposals are recorded in paragraphs 13(v) and 16(ii) of your Note of 2 July to E(DL) under reference 79(6).

2. My own view is that it would be unwise to go ahead with either of these proposals. I understand that your Legal Adviser minuted you to this effect on 5 July and in substance I agree with all he said.

3. On the proposal to negotiate out of the sixth round "carried interest" arrangements -

(i) Might this not result in BNOC having to bear a greater proportion of the costs of exploring for oil in any licensed area which turns out to be unproductive, and hence in extra costs for the Exchequer, on which I would expect the Chancellor to have views? Furthermore, would not rights to the oil from any productive field be foregone, which would mean losing a possible future advantage to the Exchequer? I realise that these are not legal points, but they may be of some importance.

(ii) Renegotiation at this stage would I understand be difficult and time consuming. Again this is not a legal point, but it has implications for staffing.

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01-405 7641 Extn

(iii) It could be argued that letting the relevant sixth round licensees "off the hook" in this way would alter ex post facto the basis on which the licences had first been offered and the original exercise of the discretion in granting those licenses could thus be called into question. In practice it would be difficult if not impossible to quantify the effect that offers to "carry" BNOC interests had in the first place on the distribution of licenses, and I cannot say what the likelihood is of legal proceedings by aggrieved parties or what the outcome of such proceedings might be. However, I think it is important that you should not act in a way which might be seen to alter in retrospect the criteria which had been used in dealing with applicants.

4. On the proposal that BNOC should relinquish its equity interests in sixth round licensed areas -

(i) The result would surely be that the other partners would have to bear a heavier burden of exploration and development costs.

(ii) The burden could I suppose be so great as to prevent some of the other partners from taking an assignment of the BNOC interest so that it would eventually pass to an outsider not favoured by the licensees who remained. In that case subsequent problems could not be resolved by negotiation with the Secretary of State since BNOC would then be out of the picture; and I can well see the original partners arguing that the basis on which they had decided to participate had been changed unilaterally and in circumstances over which they had no effective control.

SECRET

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5. For these reasons I would much prefer that these two proposals were not taken on board.

6. I am copying this to the Prime Minister, all members of E(DL), the Lord Privy Seal, the Secretary of State for Scotland, the Lord Advocate and Sir John Hunt.

Yours ever.
Michael.

The Rt. Hon. David Howell, M.P
Secretary of State for Energy.

10 DOWNING STREET

Note for file.

The only copy of L.C.A. of E(DL)(79) 3rd Mtg Minutes – Thursday 5 July 1979 is filed on Econ. Pol. June 1979; Disposal of Public Sector Trading Assets

Ref: A09903

PRIME MINISTER

STATE INVOLVEMENT IN THE OIL INDUSTRY
E(DL)(79)6

BACKGROUND

This paper by the Energy Secretary covers a lot of controversial ground. I have suggested, in my brief on the Financial Secretary's paper (Item 1) that you should touch on this at the present meeting only insofar as it affects the proposals to sell £200 million of BGC/BNOC assets in the current year. The remaining issues raised by the paper will need to be considered separately, either by E or E(EA), and it will be helpful to have your instructions on which you would prefer. Meanwhile, Sir Kenneth Berrill's note to you of 3 July, copied to all other Ministers, sets out the main points which need to be considered.

Flag A

HANDLING

You might start the discussion yourself on the lines above. You could then ask the Energy Secretary to introduce his paper, asking him to concentrate the discussion at this stage on the damage which would be done by disposal of £200 million worth of assets.

That damage will be minimised if he is prepared to sell BGC's Wytch Farm on-shore oil field, for £100 million. This means standing up to a row with Sir Denis Rooke. (The trouble is that, at Budget time, he gave Rooke a half promise that his programmes would not be further affected at least this year). If he is not prepared to do this, then he has, on his own reckoning, got between £80 million and £150 million (with a 'central' estimate of £130 million), in hand from the sale of BNOC interests in Viking and Statfjord. (The Treasury paper says £100-£130 million). He offers to find the balance of the £200 million from somewhere else. Where would he find it? To whom would the assets be sold?

When? (It must be in the present year). Would BP be interested? What damage would these sales do to the oil policy objectives set out in his paper? (Provided BP were the purchaser, or possibly Shell, the damage in terms of effect on disposals of oil could be reduced - but equally a restricted sale might reduce the price obtainable).

You might then seek views from the Lord Privy Seal and from the Chancellor of the Exchequer or the Financial Secretary: Mr Howell's arguments may need probing if he is unclear about the additional assets he would sell (we understand he has a list in mind) or makes unspecified difficulties of the kind hinted at in his paper (paragraph 19). Just what are the political difficulties, and do they matter? Would retention of these interests in British hands damage the sale price (ie can British oil companies afford to buy them); what would they do with the oil? Would the disposal require legislation if Lord Kearton refused to co-operate? (The Attorney General thinks it may). If so, could it be introduced in time; or might it be tacked on to the Industry Bill or included in an omnibus bill? (See Mr Howell's letter of 3 July to the Financial Secretary).

CONCLUSIONS

I suggest you reserve conclusions on this paper until you sum up the end of the whole meeting - see brief on main paper.

MJV.

pp

JOHN HUNT

4 July 1979

Ref: A09902

SECRET

PRIME MINISTER

Disposal of BNOC Assets to BP
(EDL)(79) 7)

BACKGROUND

This proposal has been included at the request of the Financial Secretary, in order to give a possible alternative to the sale of BP shares (and to a lesser extent as a means of avoiding sales of BNOC assets to non-British companies). BP may well in any case prove to be the purchaser for Viking and Statfjord. The proposal here is to sell all BNOC's other major up-stream assets to them (at a price of perhaps £750 million). The advantage of this proposal would be to retain some Government control of the assets via BP, and to make sure that they did not pass into foreign hands. The disadvantages are that control through BP is less direct than through BNOC (indeed despite, or perhaps because of, the Government shareholding BP tend to be very independent of Government) and that it is much easier to secure control of North Sea oil supplies to the United Kingdom through BNOC than through BP without falling foul of the EEC Commission. It is also probable that, even if BP could afford the immediate cash outlay (which would involve a rights issue which Her Majesty's Government would presumably forego) BP's own shares would go down considerably in anticipation of the heavy capital outlay involved in developing these ex-BNOC fields. Sir Kenneth Berrill points out, in his minute to you of 3rd July, some of the other disadvantages of this course. I understand that the Financial Secretary will not wish to pursue it, and Mr. Howell certainly does not propose it seriously.

HANDLING

2. You might begin by asking whether anyone wishes to pursue this option. If they do, then you could (with the briefest of introduction from the Secretary of State for Energy) consider the merits of the case: the problems include:-

(i) Would BP want the assets, and how might they be persuaded to buy them?

(ii) How would BP raise the money? If by a rights issue, what would the Government do?

(iii) How would the purchase look to other oil companies: would they complain that they were not been given a fair crack of the whip?

(iv) What would be the effect on BP's standing in the oil world? Will it look too much like an agent of Government in future?

(v) What is the case for retaining a rump BNOC, once all its major assets have been sold to BP? Will this not make the participation agreements look even more transparent, and thus weaken the control over oil disposals?

CONCLUSIONS

3. The most likely outcome is the agreement to drop this proposal. If not, you might revert to the point at the end of the meeting - see main brief.

John Hunt

4th July 1979

EA JUL 1979

Ref: A09902

SECRET

PRIME MINISTER

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(EDL)(79) 7)

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CONCLUSIONS

3. The most likely outcome is the agreement to drop this proposal. If not, you might revert to the point at the end of the meeting - see main brief.

John Hunt

4th July 1979

Subject file
Econ Pol - May 79 - Pepper Mtgs

CONFIDENTIAL

Energy : ANOC

NOTE OF A MEETING BETWEEN THE PRIME MINISTER AND MR. GORDON PEPPER at 11.45 A.M. ON WEDNESDAY 4 JULY

The following are the main points which came up in discussion.

I. Asset Disposals

The Prime Minister asked Mr. Pepper for his views on the sale of BP shares. She was particularly worried about the timing of the sale, and whether it would be right to sell any shares outside the United Kingdom. She had earlier taken the view that all of the sale should be in the United Kingdom in order to mop up liquidity and thus have the greater impact on the money supply. But the Treasury were arguing that some sales would be desirable abroad because this would allow a higher overall price, and in any case domestic sales would to some extent be a substitute for sales of gilts. Mr. Pepper said that there was likely to be some substitution between gilts and BP share purchases. But there was a trade-off between higher interest rates and selling these shares in the United Kingdom: the larger the share sale, the smaller the amount of gilts that would have to be sold, and therefore the lower the yield. It would be a mistake, in his view, to flood the London market with, say, £1 billion of BP shares - this would only depress the price. There were various methods of undertaking the sale - for example the market could be "tapped" continuously over an 18 month period rather than in one or two tranches. However, this was a highly technical matter and in any case an extension of the sale over 18 months would not meet the Government's funding requirement. The Prime Minister commented that from a political standpoint it would be better to sell the shares in the United Kingdom, and she still felt it would be better on money supply grounds. However, she understood that, even if the sale did take place entirely in the London market, foreigners would still be able to make purchases. Perhaps a preference should be given in the first place to United Kingdom nationals. Mr. Pepper said that this would not stop foreigners from buying the shares, because a secondary market would quickly develop. He cited the example of the BP sale in 1976: many of the shares which had been sold in

/New York

New York had subsequently been bought by United Kingdom institutions Mr. Pepper went on to say that Mr. Tom Quinn would be a good person to advise the Government on the details of the sale, although he was sure that the Government was already taking advice from the Merchant Banks.

SECRET

Original on Econ Pol: June 1979 Disposal of Public Sector Assets

4

Ref. A09900

PRIME MINISTER

Disposal of Assets

(E(DL)(79) 5)

BACKGROUND

You decided to take over the chair of this meeting of the Sub-Committee yourself. (Mr. Lankester's letter of 25th June.) This followed from an unresolved discussion about the "some £1 billion" of asset sales which the Chancellor promised in the Budget Speech to find this year. Your concern was mainly about the timing and the extent of the proposed sale of BP shares. At the same time, the Secretary of State for Energy was concerned about the proposed disposals of BGC and BNOC assets. He has since circulated a major paper (Item 2) (E(DL)(79) 6) about the future of BNOC. A substantive discussion of oil policy, including the role of BNOC, will be necessary at a later stage but to pursue it now would be to complicate an already complex discussion. Tomorrow's meeting could therefore be confined to the possibility of disposals without damaging the Government's oil policy objectives. For that reason, I have placed the Financial Secretary's paper first on the agenda, and suggest you use it as a framework for the meeting. You will need to look at Mr. Howell's papers against that background.

You will remember that the Chancellor's Budget target came down from disposals of £1.2 billion to £1 billion, largely because of problems over the BGC and the BNOC assets. The doubts about the BP sale were voiced subsequently, after the Chancellor had made it clear that BP would account for a substantial part of his total. A number of other Ministers have suggested alternatives, but none of these add up, in total, to anything like the sum required. To achieve that target will require the sale of a large slice of the present BP holding, or alternatively the sale of most of the BNOC assets to BP (dealt with in the second paper from the Secretary of State for Energy). The arithmetic is set out in an Annex to this brief.

HANDLING

You will want to start by inviting the Financial Secretary to introduce his paper. It falls into two halves: the arithmetic of the £1,000 million (see Annex again) and the mechanics of the BP sale; and so might the discussion.

I. Options for raising £1,000 million

It will be best to run through the possibilities mentioned in paragraphs 2-8 and set out in more detail in Annex A. You will want to avoid becoming bogged down with those sales which cannot contribute to the 1979-80 PSBR.

(a) National Enterprise Board

The proposals are agreed: but the legislation may be difficult. It will form part of the Industry Bill. The Secretary of State hopes to introduce this in November and get Royal Assent by January. That in itself would be difficult, as QL recognised. But he has not even got policy clearance yet for the other parts of the Bill, some of which are quite controversial (especially those dealing with the regional activities of the NEB). If you score this £100 million therefore, you should make it clear to the Secretary of State that he must press ahead urgently with his legislative proposals.

(b) Suez Finance Company

No legislation needed. Sale this year cannot be guaranteed.

(c) British Sugar Corporation and Covent Garden Market Authority

Neither of these needs legislation. Some part of the proceeds would be needed to offset other expenditure by MAFF. But the Treasury are reckoning on £15 million being available for the disposals package.

(d) Land (paragraph 16 of Annex)

The Secretary of State for the Environment has promised £30 million firm (including the £20 million on New Towns mentioned in the letter of 2nd July from the Chancellor's office), without legislation. We know he has something else up his sleeve, but he has so far refused to specify what it is. (We think he wants to offer it in exchange for some modification of the BP deal.) This is very unsatisfactory: if he makes a

firm proposal at the meeting, you will want to insist that it is something which does not require legislation, or can be tacked on to legislation which will get Royal Assent in time to show results in 1979-80. Otherwise, it does not score in this package, however useful it may be for later years.

(e) British Steel Corporation

No problem - no legislation needed.

The remaining proposals are listed in Annex A, but none of them can produce savings in 1979-80. You may not want to waste much time on them. Points arising are:

(f) Cable and Wireless

The Treasury view is that this will not actually yield anything in the current year.

(g) British Airways

Mr. Nott raised this possibility with you two weeks ago. It requires legislation, for which there is no provision in the programme. (He is making a last-minute attempt to fit it in, and the Chancellor of the Duchy and the Chief Whip are resisting. There is a separate paper, E(DL)(79) 4, on this prospect: but it does not help in the present year unless the Chancellor of the Duchy and the Chief Whip relent. If after considering his paper (Item 4) the Sub-Committee did want to pursue this possibility, you would have to instruct that room be found for it in the programme, and that Mr. Nott should urgently seek policy clearance for his proposals. A further meeting of E(DL) under the Chancellor of the Exchequer could deal with those.

(h) British Aerospace

This too needs legislation, and there are important policy decisions not yet taken. It seems unwise to count on this in the present year.

(i) British Shipbuilders

This seems even more unlikely than British Aerospace, within the current year.

(j) Radio Chemical Centre

Unlikely to yield very much; together with the next item, £15 million at most.

(k) National Freight Corporation

The Treasury have not scored this one either: although the legislation could be available in time, it does not seem a sensible option and only yields about £15 million. We have not thought it necessary to invite the Minister of Transport for this item.

(l) British Rail

Again this requires legislation and could not be in place in the current year.

(m) Forestry Commission

Legislation again: no provision in the programme.

If the Financial Secretary's bids in paragraphs 2-6 are confirmed, he has now got about £180 million available, and needs a further £820 million. This can come only from sales of BNOC/BGC oilfield assets, and/or from the Government's stockholding in BP.

(n) BNOC and BGC

The Financial Secretary's bid is for £200 million from these two combined. The Secretary of State for Energy, in his own paper on BNOC, offers to find the £200 million, but only specifies two fields (Viking and Statfjord) which together he puts at a range of £80-£148 million. (The Treasury paper says £100-£130 million.) The Treasury suggest the BGC onshore oilfield at Wytch Farm (Dorset); this will yield perhaps £100 million. But the Secretary of State for Energy is reluctant to face the row with the BGC. Legal advice is that he has the powers to direct the Corporation to make this sale. If he is not prepared to do so, then he is driven back on finding the whole £200 million from BNOC, which he is only prepared to do "providing that the legislative difficulties can be overcome and that this is consistent with our overall decisions for the future of BNOC" (paragraph 18 of his paper, E(DL)(79) 6). You might tentatively score £200 million at this stage, and then come back to this option later in the meeting if necessary, following discussion of his paper at Item 2.

(o) Sale of BNOC Assets to BP

This too is the subject of a separate paper - E(DL)(79) 7 (Item 3). The idea is to sell sufficient of the BNOC assets to yield about £750 million to BP, leaving a rump BNOC behind to deal with participation oil, manage any remaining equity interests, and (subject to discussion of the next paper) carry out any other functions assigned to it by Government. This is probably a second-best to the proposed sale of BP shares. You will want to defer a decision on this, too, until the Sub-Committee has taken the Secretary of State's paper, and then revert to this point at the end of the meeting.

At this point you might look at the legislative implications. None of the smaller items above looks especially attractive as an immediate option. The legislative programme, as you know, is already very crowded. But if you were forced to scrape the barrel, and include many of these in a disposals package, it would then be worth amalgamating them into an omnibus Bill and guillotining it through soon after the Recess. This would at least ensure that some sales would go through in the current financial year. If necessary you might ask the Financial Secretary to reconsider this idea (which he has previously rejected) and report to you on the possibility.

II. Sale of BP Shares

This is the main part of the paper, and the most difficult. You have already had some discussion with a few of the Ministers concerned. There are five points to establish at the beginning:

(i) Sale of shares does not, of itself, affect Government control over BP, provided it retains the right to block an amendment of the Company's Articles. Technically that requires 25 per cent; in practice, 15 per cent will be enough.

(ii) The Government and the Bank between them presently own 51 per cent, of which 20 per cent came from Burmah. We believe that any attempt to sell ex-Burmah shares would simply provoke Burmah to seek an injunction forbidding the sale, and that this would probably be allowed. So in practice there is only 35 per cent of the equity to play with. The Chancellor's proposals involve selling approximately 20 per cent. This would still leave enough to block any change in the control of the company.

(iii) In practice, ownership of the shares have made little difference to Her Majesty's Government's control over BP: if anything, they are more difficult to deal with than Shell.

(iv) Whatever the fine print says, there is no way in which the Government can stop the shares passing into foreign hands. They are widely traded internationally already. But this has nothing to do with the destination of BP's oil. This is much more dictated by their international trading commitments. Put bluntly, if we cannot control what BP does with its oil, no foreign owner is likely to do better.

(v) As regards the future price of BP shares, the problem is one of timing. Some Ministers have argued that the Government would get a better price by deferring the sale. In the long term, that is probably true, as the world oil price moves up in real terms in the '80s. But in the short term, although oil shares have risen since the OPEC increase, the effect of that increase may be to slow down the world economy and weaken the market for oil. To defer the sale till next year would risk a lower price. And in any case the Chancellor's arithmetic requires a sale this year, unless an acceptable alternative can be found.

Nigeria.

Having established these points, there are really five questions to which the Committee should turn: do we sell the BP shares; how much do we sell; when; to whom; and how? All these points are carefully covered in the paper. The main point to watch is the need for an early decision: unless you can reach agreement virtually at this meeting (perhaps with one or two tiny loose ends left over for separate negotiation) we shall lose the July option altogether, and the price may turn against us.

Having covered the ground on BP, you may then want to turn to the other three papers on the agenda, to make sure that the other options have all been considered properly before attempting to sum up.

CONCLUSIONS

(To be recorded at the end of the meeting, after Items 1, 2, 3 and 4.)

This will depend very much on the way the meeting goes. If the decision is to proceed with the BP sale, then the conclusions might be:

(a) To note that, of the £1 billion sales announced in the Budget, £100 million will come from the disposals of NEB shares, and £30 million from disposals of public sector bodies under the Secretary of State for the Environment.

(b) To agree that a further £50 million should be found if possible from sales of the Suez Finance Company, British Steel Corporation assets, and Government shares in the British Sugar Corporation and the Covent Garden Office Block.

(c) That a further £200 million should be found, by whatever means the Secretary of State for Energy thinks best, from BGC and BNOC assets.

(d) The balance of the £1 billion should be found by selling sufficient of the Government's stockholding in BP to reduce it to about 35 per cent (including the ex-Burmah 20 per cent), the timing to be decided between the Chancellor of the Exchequer and yourself.

(e) That a proportion of the BP stocks should be offered for sale in New York and one other centre abroad; that preference should be given to BP employees and small investors; and that the BP proposal for United Kingdom employee participation should be pursued urgently between the company and the Treasury.

(f) That the wider issues raised in the Secretary of State for Energy's paper on BNOC be considered at a later meeting of the Committee.

(g) That E(DL) should consider further the issues raised in the paper by the Secretary of State for Trade on British Airways.

If the decision goes against the sale of the BP shares, or some part of it is modified, conclusions (d) and (e) might be replaced by:

(h) EITHER that up to x per cent of the BP shareholdings should be sold, and that the balance of the £820 million should be found by the sale of BNOC assets to BP; OR that the whole of the £820 million or as much as possible should be found from the sale of BNOC assets to BP, if necessary leaving a shortfall on the target of £1,000 million.

And in addition, subject to the course of discussion, possibly:

(i) To agree that additional sales of assets in /British Aerospace, etc./ should be added to the list of disposals to produce the total of £1,000 million; and to invite the Financial Secretary, Treasury, to report to you urgently on the possibility of an omnibus Bill to give legislative authority for these disposals early after the Recess.

pp. JOHN HUNT

4th July, 1979

ANNEX

		£m
1.	**Sales already agreed**	
	NEB subsidiaries	100
	Land and buildings (New Towns etc.)	30
	British Steel	15
	British Sugar Covent Garden Market	15 net
	Suez Finance Company	20
		180
	Gap to be filled	820
	Total	1,000
2.	**Other possibilities in 1979–80**	
	BGC – Wytch Farm	100
	Either: BNOC – Viking BNOC – Statfjord Other BNOC disposals	Say 120–130 up to 200
	Or: Sale of BNOC assets to BP	up to 750
	Or: Sale of BP shares to public	about 620
3.	**Other possibilities, probably later**	
	Suez Finance Company	20–25
	Cable and Wireless (half)	100
	British Airways (half)	150
	British Aerospace (half)	100
	British Shipbuilders	35 net
	Radio Chemical Centre Ltd National Freight Corporation	less than 50
	Britsh Rail – Sealink etc.	25–50
	Forestry Commission	?

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SECRET

Qa 04172

To: PRIME MINISTER

From: SIR KENNETH BERRILL

State Involvement in the Oil Industry:
Future Arrangements

1. In his review of BNOC's activities (E(DL)(79)6), the Secretary of State for Energy advocates slimming down BNOC so that the United Kingdom's essential national needs are served without unnecessary state involvement in the oil industry. The CPRS suggests that when Ministers discuss how this objective can best be achieved they might bear in mind the following.

Overall Strategy

2. The Secretary of State is on firm ground in arguing that a state organisation of some kind is necessary for the effective implementation of North Sea policies. The objectives of the multinational oil companies will not always coincide with those of the nation and there must be an effective counter-balance. This is recognised by every major oil producing country in the world. Indeed, the extent of the United Kingdom Government's control is already less than in most other oil producing countries, including, for instance, the United States.

3. At the moment security of supply overshadows all other reasons for continuing with a BNOC. But there are other reasons which are very cogent. Through a BNOC the Government is able conveniently to exert influence in such important areas as the rate of development of our oil resources, the opening up of reserves in much deeper water, staking our claim in disputed territory, giving some preference to United Kingdom industry in orders for offshore supplies. In general, a BNOC can be an invaluable source of information and advice to central Government on what, in detail, is happening in the exploitation of the oil reserves of our Continental Shelf - not least in the areas of costs, profits, and potential taxability.

Participation Agreements

4. The CPRS fully supports the Secretary of State's recommendation that we should retain BNOC's options to participation oil and, less importantly, to royalty and equity oil (the latter at a reduced level). This ability to take crude oil is of immediate importance in the scope it provides for avoiding the presentational and substantive embarrassment of the United Kingdom experiencing shortages of refined products at a time when the public is only too well aware that we are approaching self-sufficiency in crude.

5. We imagine Ministers will wish BNOC continuously to exercise its options to take crude oil. It is impractical to think of BNOC only exercising its options at times of shortage, because

- BNOC is bound to give the companies six months' notice of its intentions; in many cases a year. Crises blow up more quickly;
- it would be difficult for BNOC to maintain the necessary expertise and to find customers if they were to be marketing, say, 5m. tonnes of oil in one year, 30 m. tonnes the next and then back to 5;
- such manoeuvres would undoubtedly be seen as an affront to EEC rules and thereby negate one of the presentational advantages we are seeking to secure.

6. It is also important that participation arrangements should be negotiated for BNOC in all future licensing rounds. (The Secretary of State's note is not precise on this point.)

Advisory Role

7. The oil business is very complex. If Ministers are to optimise the national interest in the North Sea they should not cut themselves off unnecessarily from a source of expert and reasonably objective advice. BNOC is building up an advisory capacity which would inevitably be greatly

E3 JUL 1979

reduced if it did not sit on all Operating Committees, especially if this were coupled with the proposed curtailment of BNOC's equity role. The best solution might be to revoke BNOC's statutory duty to advise the Government, but to retain BNOC's seat on the Operating Committees.

Disposals

8. The introduction of private capital through the sale of shares in appropriate BNOC interests is an attractive proposal and, subject to the Chancellor of the Exchequer's Budgetary needs, is preferable to the out-right sale of BNOC's assets, because (a) it should be easier presentationally, (b) it should be possible to ensure that more of a stake remains in British hands, and (c) BNOC would retain more upstream expertise (especially important if they no longer sit on the Operating Committees in which they have no equity interest).

9. The proposal examined by the Secretary of State in E(DL)(79)7 to dispose of all BNOC's assets to BP appears to offer few advantages and a considerable loss in terms of security of supply. Accordingly, we agree with the Secretary of State that the idea should not be pursued further but that BP should be regarded as a useful potential purchaser for part of BNOC's upstream assets according to the Chancellor's PSBR requirements.

Conclusion

10. In short we believe Ministers should support the broad strategy identified in the Secretary of State's paper, with the provisos that they should consider

- BNOC exercising continuously its rights to take crude oil;
- BNOC remaining on all Operating Committees so as to maintain and improve the flow of information and advice to central Government.

11. I am sending copies of this minute to Ministers on E(DL) Committee, and to Sir John Hunt.

KJ

3 July 1979

COPY No OF COPY No 11 OF 11 COPIES

COPY NO 1 OF 11 OF 11

E 2

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

01-211 6402

SECRET

3 July 1979.

Nigel Lawson, Esq., MP,
Financial Secretary to the Treasury,
HM Treasury,
Whitehall SW1.

Dear Nigel

DISPOSAL OF ASSETS

Thank you for your letter of 12 June. Most of the points you raised in it were discussed at E(DL) on 20 June, but I think it worth writing to emphasise the timetable difficulties with regard to BNOC.

As I indicated at E(DL) any decisions with regard to the raising of money from sales of BNOC assets is one that we will need to take in the context of wider policy decisions about BNOC; and I am on the point of putting proposals to colleagues on this question. However I am clear that if colleagues agree to sales then legislation will be needed, as I can see no way of circumventing the legal difficulties described by the Attorney General. You suggest that in these circumstances we introduce the necessary legislation as part of the Bill which I am planning to implement the conclusions of my Review of BNOC. This is clearly a logical place to put such legislation, but I have no confidence that we could meet the advanced timetable that you are proposing. But until the future policy with regard to BNOC is established there can be no question of setting in hand detailed preparations for a Bill. I think therefore that it would be unrealistic of me to give you any hope that the Bill could be ready for introduction immediately after the Summer Recess. Indeed my original target date for introduction just prior to the Christmas Recess was based on policy decisions being taken by mid to end July. I suggested at E(DL) that to be sure of achieving the earliest possible timetable it may be sensible to tack a clause onto the Industry Bill alongside that dealing with NEB. It seems to me important that whatever decisions we take on, we should proceed in a way which keeps our options fully open as to the method of disposal.

I am copying this letter to other Members of E(DL), the Attorney General, the Lord Advocate and Sir John Hunt.

Yours ever
David

D.A.R. Howell.

END

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