

Confidential File

Study of New Gas gathering  
Pipeline in the North Sea.  
Appointment of Sir Denis Rooke as  
Chairman of the Organising Committee

ENERGY

JULY 1979

Referred to	Date	Referred to	Date	Referred to	Date	Referred to	Date
<del>7-7-79</del>		14-9-79					
<del>20-8-79</del>							
<del>4-6-80</del>							
<del>10-6-80</del>							
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PREM 19/454

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**Cabinet / Cabinet Committee Documents**

Reference	Date
<i>E(80) 52</i>	<i>6.6.80</i>
<i>E(80) 19th Meeting, Minute 2</i>	<i>11.6.80</i>

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 *A Wayland*

Date *31 March 2011*

**PREM Records Team**

## 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,

19 June 1980, columns 596 - 598

"Written Answers: Gas Gathering (North Sea)"

Signed A Wayland Date 31 March 2011

**PREM Records Team**

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PC 15

SUBJECT

cc Nationalized Industry Steel  
cc member



cc Mr. Walters  
Mr. Ingham

10 DOWNING STREET

From the Private Secretary

14 September 1981

RF X

Dear Peter,

As you know, Mr. Ian MacGregor called on the Prime Minister last Wednesday afternoon. He was accompanied by Mr. Tebbit.

Mr. MacGregor said that BSC's performance during the current financial year was to some extent off course. Their expectations about the domestic market had proved rather too optimistic - mainly because the recession in the construction and engineering industries had proved longer than they had anticipated. They had managed to maintain their volume of production by "buying" exports; but as a result they had eaten into their contingency reserve. BSC were hoping to increase their exports to the USA. The prospects were reasonably favourable. He had seen Mr. Baldrige, the US Secretary of Commerce, who had indicated that the Administration was likely to accept higher imports from the UK provided that other European producers did not continue to dump steel which they were unable to sell in Europe on the American market. BSC had a reasonably good case for increasing their exports to the US, particularly since they had been exporting to that market at a considerably higher level in the early 1970s. Also, unlike the Europeans, they had been concentrating on special steels, which posed less of a threat to the US steel producers than the bulk steels. BSC would continue to be selective in their efforts to penetrate the American market, and he would shortly be having talks with Viscount Davignon to try to ensure that BSC's efforts were not thwarted by their competitors in Europe.

Mr. MacGregor mentioned briefly his proposals for the coming pay negotiations with the steel unions. He hoped to persuade them that there should be no general pay increase, but that there should be bonuses at plants that performed well. There was then some discussion of BSC's investment and capacity problems. Mr. MacGregor said that much of BSC's investment in recent years had been mis-directed: he mentioned in particular that there had been too little investment in tube making capacity. A major problem at present was the future of the Redcar blast furnace: it was uneconomical to keep this furnace going since there was no second furnace next to it which could be used while it was periodically relined. Mr. MacGregor also mentioned the problems of GKN's Brymbo plant, which BSC had an interest in seeing closed. This made sense insofar as it was probably the worst plant of its kind in the industry, but closure would be expensive. In response to a question from the Prime Minister about the future of Sheerness, Mr. MacGregor said that

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- 2 -

their problem was essentially lack of demand; BSC were trying to persuade the Canadians to close Manchester Steel, which would help Sheerness.

Turning to the coal industry, Mr. MacGregor said that it was essential that NCB should close down their uneconomic pits, particularly those in South Wales. He thought that the best approach to persuading the unions was for the Government to publicise the appalling conditions in the South Wales pits. The public would never support their continued working if the conditions in them were better known. Mr. MacGregor also warned about the technical problems of building up coal at power stations: he hoped that the Government appreciated that coal tended to oxidise and lose calorific value the longer it was stored.

Mr. MacGregor said he hoped the Government would consider favourable the latest proposals from the consortium headed by BSC for the Channel crossing link. The fundamental problem in obtaining private sector finance for the project was somehow to guarantee its completion. The same applied to the gas gathering pipeline project; but for the latter to attract private finance, it was essential that BGC should no longer be the monopoly purchaser of gas flowing through the pipeline. In addition, BGC's monopoly in selling industrial gas should be removed, and the transport of gas on-shore ought to be on a common carrier basis. The Prime Minister asked if Mr. MacGregor would write to her with his proposals for the gas gathering pipeline. (In the event, he wrote to David Young - a copy of his letter is enclosed and the Prime Minister would be glad to know of the outcome of the meeting which Mr. MacGregor is to have with Mr. Young on it.) One final point that Mr. MacGregor made was that, for large scale projects that the Government wished to see financed by the private sector, it should consider providing specific tax exemptions to those who put up the funds: this had been successfully done in the US.

I am sending a copy of this letter and the enclosure to Julian West (Department of Energy) and John Kerr (HM Treasury) and without the enclosure to Tony Mayer (Department of Transport).

*enc.*

*Tim Lambert*

Peter Mason, Esq.,  
Department of Industry.

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*no news  
of the offer  
in 1974  
has made  
the same*

14 September 1981

Many thanks for the lunch on Friday which I very much enjoyed.

Thank you also for sending over a copy of Ian MacGregor's letter to David Young about the gas gathering pipeline. I have shown this to the Prime Minister, and she has noted that you are seeing David about it tomorrow.

TPL

David Prior, Esq.



010

**British Steel Corporation  
Head Office**

P.O. Box No. 403, 33 Grosvenor Place, London SW1X 7JG  
Telephone 01-235 1212 Telex 916061



11 September 1981

Mr T Lankester  
Prime Minister's Office  
10 Downing Street  
LONDON  
SW1

Dear Tom,

... As promised I attach a copy of Mr MacGregor's note to David Young. Mr MacGregor felt that in the first instance it would be best to go through Mr Young rather than bother the Prime Minister. We have a meeting with Mr Young on Tuesday 15 September.

I enjoyed our lunch and will look forward to seeing you before too long.

Yours sincerely

Yours truly  
David

David Prior

BRITISH STEEL CORPORATION

2

IAN MACGREGOR

Thanks  
MJK

Arranged for  
Tues 15th Sept  
@ 19.00 here

cc Mr. Watson  
N. Walker

11 September 1981

Prime Minister

This is the letter which  
Ian MacGregor promised  
to send. It is addressed  
to David Young, whom  
he will see about it next  
Tuesday. I will  
keep in touch.

Mr D Young  
Department of Industry  
Ashdown House  
123 Victoria Street  
LONDON  
SW1E 6RB

Dear David

When I met with the Prime Minister on Wednesday we discussed the Gas Gathering scheme and the failure so far to devise a financing package which did not fall within the public sector borrowing requirement. I told her that I believed that it was perfectly feasible to finance the scheme with private capital.

Tuesday. I will  
keep in touch.

The essential ingredient would be to establish a private sector pipeline company operating and financed on a strictly commercial basis. Such a company would have the right to negotiate gas supply contracts from the producers, the right to distribute the gas domestically through the existing transmission system (for an economic tariff) and the rights to sell the gas. In this way the pipeline financing would be arranged along similar lines to the pipelines in the USA with which I am very familiar.

N  
11/9

British Steel Corporation has a very keen interest in seeing this project proceed and, if privately financed, such a project would clearly be in the overall interests of the United Kingdom. I have asked Ian Fraser, the Chairman of Lazard Brothers, to put together the preliminary outline of a scheme and I am attaching his ideas.

Ian Fraser and myself would like to visit with you and whoever you think is appropriate to see whether we can get this project on the road again as soon as possible. I will ask my secretary to be in touch with your office to see if we can find a mutually convenient time.

Sincerely

Ian

cc: Mr. Ian Fraser - Lazard



## GAS GATHERING SYSTEM

### Discussion Paper

1. A reduction in the role of Government in the project and a financing scheme that falls outside the PSBR.
2. A modification of the role of British Gas Corporation, so as to feature in the project as a purely commercial, albeit important, participant.
3. As part of 2. above, British Gas Corporation would no longer be the monopoly purchaser of gas flowing through the pipeline; the price formation for the relevant gas would be determined by market forces.
4. Sponsorship and ownership of the pipeline company by the participants, who would include the producing oil companies and certain large industrial consumers such as the refiners, British Gas Corporation, British Steel Corporation, The Distillers Company Limited, ICI Limited, etc. Control and operating responsibility to flow from ownership.
5. The critical completion guarantees to be provided on a conventional basis by the participants in proportion to their participations.
6. Primary finance (i.e. until completion of construction) to be provided by the banking system under the umbrella of the completion guarantees. Upon completion, the primary finance to be replaced by long-term debt finance secured upon throughput commitments.
7. The throughput commitments mentioned in 6. to be undertakings to use in the pipeline and pay for that use at the ruling tariff. The tariffs to be such as to enable the financing of the pipeline to be paid off together with a reasonable return on the participants' capital. Commercially and politically acceptable machinery to be constructed for tariff determination (c.f. Civil Aviation Authority).

8. The principal attractions of the line of approach are that it involves a return to market principles, it reduces Government intervention, and it limits the commitment of Government credit (i) directly to zero, and (ii) indirectly (through British Steel Corporation, British Gas Corporation and BNOC) to internationally normal and fully commercial levels.

*Energy*

The Government has now completed an examination of the benefits and costs of an integrated gas gathering pipeline scheme, and compared them with the benefits and costs of the alternative of allowing companies to bring ashore gas from the North Sea through arrangements of their own, as a number of them would prefer.

It is clear that the vast bulk of the gas reserves will be brought ashore under either arrangement. Oil companies like the Government have been attracted by the concept of the integrated pipeline and have now had a year to examine its implications. It is now possible for a balance to be struck between the benefits and costs offered by each approach.

One of the conditions which made the integrated scheme in principle attractive was that the oil companies would have borne most of the costs and risks. But it has emerged that the conditions which would be needed in order to make an integrated scheme attractive for oil companies to invest in would have entailed constraints which were unacceptable to the Government.

It is now clear that if the integrated line was to have proceeded according to the necessary timetable, it would have had to be owned and financed at least initially, and perhaps for some years, by the public sector. While there would have been some additional benefits with the integrated line, these were not sufficient to outweigh the extra burdens and risks involved.

/ The integrated

The integrated scheme would have involved an earlier and possibly larger burden on the PSBR. On the other hand, development by the oil companies will involve a cost to the PSBR through tax offsets in later years. Accordingly, the PSBR effects were not a major factor in the decision.

The integrated scheme would have entailed the commitment of capital a considerable period before this in order that sufficient gas would be committed to the pipeline. Inevitably, the risks would have been concentrated, and largely borne, in the public sector.

Leaving the companies to make their own arrangements for bringing the gas ashore has the advantage that facilities will be provided in the light of market conditions and the increased knowledge of gas reserves. This follows the pattern that has been successfully followed for the exploration and development of North Sea oil.

The absence of an integrated scheme would reduce the opportunity of bulking natural gas liquids including Ethane particularly in the early years. but at present the market is extremely slack due to great overcapacity in the European Petrochemical Industry and this is likely to continue for the foreseeable future. However, today's decision frees companies to make their own arrangements in this respect in response to market demand.

At first sight it might appear that not having the integrated scheme would result in a reduction of job opportunities. However, other opportunities will result from the arrangements made by industrial oil companies to land the gas. Moreover, any extra public spending involved in the integrated scheme would have needed to be offset by cuts in public spending elsewhere.

Going ahead with the integrated line could have resulted in under-utilisation of the existing facility in Scotland, e.g. the Flagg and Frigg lines.



cc  
Press Office

~~Mr. L. H. ...~~

Secretary of State  
for Energy

Tim Lankster  
No 10.

R

GAS GATHERING PIPELINE

I attach for information a revised version of the Secretary of State's draft press statement. He intends to issue this later today. We will let you know the precise timing by telephone as soon as possible.

JANET CHADWICK

APS/SOS

11 Sept 81

c.c. Peter Jenkins - Chancellor Office, Tsy  
Catherine Bell - SOS Industry  
B. Morgan - Mr Fletcham's Office, Scottish Office

GAS GATHERING PIPELINE - DRAFT PRESS STATEMENT

The Secretary of State for Energy announced today that the Government had completed its examination of the integrated gas gathering pipeline scheme.

The integrated pipeline project was planned on the basis that it would be a private sector utility, mainly owned and financed by the private sector, with 30% participation by BGC. However, after many months of negotiation the private sector has not come forward with proposals to invest in the scheme at the necessary levels.

It is clear to the Government that, either by the integrated scheme or by a number of separate schemes, the vast bulk of North Sea gas reserves can and will be brought ashore.

The Government has therefore decided that companies should, in the future as in the past, make their own arrangements for bringing the gas ashore. It is confident that, following the pattern which has been successfully adopted for the discovery and exploitation of North Sea oil, the producer companies will ensure that Britain's North Sea gas reserves are brought ashore efficiently in accordance with the nation's needs.

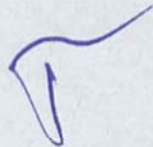
11 September 1981



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

10 September 1981

T. Lankester, Esq.,  
No.10, Downing Street



*Dear Tim,*

..... I attach an amended version of the draft statement sent over to you by Janet Chadwick earlier today, with the changes which the Chancellor would like to see made underlined.

*Yours ever  
Peter*

P.S. JENKINS



The Department of Energy announced today the Government's decision on the gas gathering pipeline project. The integrated pipeline project was launched on the basis that it would be a private sector utility - mainly owned and financed by the private sector. [It

WITH 30% PARTICIPATION BY BRITISH G.A.

is now clear that the private sector are unable to risk their money invest in the scheme.]

IN THE FUTURE AS INTD ASST

The Government has therefore decided that companies should make their own arrangements for bringing the gas ashore. It is confident that, following the pattern which has been successfully adopted for the discovery and exploitation of North Sea oil, the companies will make satisfactory arrangements [in the light of their increasing knowledge of gas reserves] which will ensure that the vast bulk of gas reserves are brought ashore. \

AFTER MANY MONTHS OF NEGOTIATION THE PRIVATE SECTOR HAVE NOT COME FORWARD WITH AN OFFER TO INVEST IN THE SCHEME.



Secretary of State  
for Energy

Tim Hancock  
No. 10 ✓

A handwritten signature in blue ink, appearing to be 'TH'.

Here is a draft of a statement  
which the Secretary of State proposes  
to make this evening

Janet Chadwick  
APS/SOS

Secretary of State for

The Department of Energy announced today the

Government's decision on the gas gathering pipeline project. The integrated pipeline project was <sup>planned</sup> launched on the basis that it would be a private sector utility and that the bulk of the finance would be provided by the private sector.

BUT  
after lengthy  
negotiations

It is now clear that the private sector <sup>will not</sup> invest in the integrated scheme <sup>has stipulated</sup> only on terms and conditions which the Government cannot accept. The Government has therefore

B.G.C

decided that companies should make their own arrangements for bringing the gas ashore. It is confident that, following the pattern which has been successfully adopted for the discovery and exploitation of North Sea oil, <sup>and some gas fields</sup> the companies will <sup>continue to</sup> make satisfactory arrangements which will ensure that the vast bulk of gas reserves are ~~still~~ brought ashore.



Secretary of State  
for Energy

Tim Hanketer.  
No 10.

Further to my earlier note, I now  
attach a copy of question & answer  
briefing.

Janet Chadwick  
APS/SOS  
10-9-81



Q: Will a more fragmented pipeline be as effective as an integrated pipeline?

A: The oil companies have a considerable incentive to ensure that they bring ashore all gas which can economically be landed.

Q: Why has it taken so long to reach a decision?

A: Huge sums of money and very complex issues are involved. Such matters cannot be decided overnight.

Q: How much money has been spent so far on the project?

A: BP, Mobil and British Gas have committed over £8m to pre-construction work.

Q: How much gas will be lost?

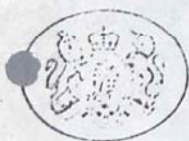
A: There is no reason to believe that any gas whose recovery is economic will be lost.

Q: Will the Norwegians be taking our gas?

A: Production licences contain a requirement that the gas be landed in Britain.

Q: How many jobs will be affected?

A: It is impossible to speculate on how many jobs will be created by alternative developments compared with the integrated pipeline. Opportunities for British industry will still be there when the oil companies come forward with their proposals.



Q: Will this mean that we cannot bring Norwegian gas to Britain.

A: We shall of course still be able to land in Britain all Norwegian gas which British Gas has succeeded in purchasing. Further supplies could be landed in Britain by existing pipelines or new pipelines if the economics were right.

Q: How will this decision affect the cost of domestic and industrial gas?

A: It will have no effect.

Q: Will there be enough natural gas to meet our needs without the integrated pipeline?

A: If the market requires extra gas supplies then it will be economic for those supplies to be developed and landed.

Q: Will this affect the development of gas fields?

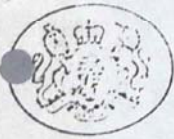
A: There may be changes in the timing of field developments, but the market will decide when the gas is developed and landed.

Q: Will this affect BGC's bargaining position with companies on the price of gas?

A: This decision relates to how gas is brought ashore not whether it is brought ashore.

Q: Will this affect the granting of licences and the timing of future rounds?

A: No.



Q: Will oil companies be able to offset construction of pipelines against tax?

A: The present tax legislation permits certain expenditure on pipelines to be offset against tax liability.

Q: What happens to N. Alwyn gas?

A: Companies have made it clear that they would land it in the UK through the Frigg line and we would now expect an application to that effect.

Jobs in Scotland	)	
Petrochemicals	)	See agreed texts

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SUBJECT

of Martin



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10 DOWNING STREET

From the Private Secretary

10 September 1981

Dear Julian,

Gas Gathering Pipeline

As you know, the Prime Minister held a meeting this morning to discuss the proposals for a gas gathering pipeline. In addition to your Secretary of State, the following were present: Chancellor of the Exchequer, Chief Secretary, Foreign and Commonwealth Secretary, Secretary of State for Industry, Minister of State, D/Energy (Mr Gray) and Minister of State, Scottish Office (Mr Fletcher). They were accompanied by officials and Mr. Ibbs and Mr. Veit (CPRS) were also present. They had before them Mr. Ibbs' minute of 8 September covering a further report as requested by the Prime Minister at the earlier meeting on 1 September, and the Chancellor's minute of 9 September.

Mr. Howell said that the CPRS report confirmed what had been known all along - that the GGP scheme would bring very substantial economic benefits, and that it was superior to the so-called multiple approach. Taking into account all the arguments that had been put forward, he remained strongly of the view that the Government should support the GGP scheme based initially on public sector finance. There was in reality no alternative scheme. Apart from the proposed Mobil line, there was no assurance that other lines would be built. Furthermore, even if they were, the multiple approach would involve greater risks of flaring, it would reduce the opportunity to bid for Norwegian gas, and there would be a substantial loss of natural gas liquids. Once launched, he believed that the private sector would soon come in to support the GGP. BP had already indicated that they would provide finance in proportion to their throughput contract, and several other companies had given similar indications. Furthermore, there was a good prospect that the private sector would help to finance the on-shore developments. For example, although they had set tough conditions, Dow Chemical had said they would finance the fractionator at Nigg Bay. The industrial implications of not going ahead with the GGP were enormous. As for the PSBR implications, these were extremely complex. But the CPRS report showed that, assuming the GGP was in due course privatised, it would result in a lower PSBR cost than multiple developments. In short, he believed the economic arguments strongly favoured the GGP. The political arguments were equally powerful. The public would find it inexplicable that the Government was not prepared to support such a good project.

/ The Secretary of State

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7



The Secretary of State for Energy went on to say that he strongly disagreed with the arguments in the Chancellor's latest minute. It ignored the fact that Ministers had already decided that an integrated line was in the public interest. He disagreed with the assertion that it would be necessary to hold back the development of Southern Basin gas in order to provide sufficient throughput for the integrated line. It was no longer true that the BGC Chairman was unwilling for BGC to accept financial responsibility for the scheme if their monopsony was removed. He was still insisting on first access to the gas fields that were essential to the success of the project, but he had dropped his reservations about the ending of BGC's monopsony position in general. He also disagreed with the argument that going ahead with an integrated line would make the UK more vulnerable to interruption of gas supplies: the amount of gas coming through the line would be considerably less than the amount already flowing through the Bacton system.

The Chancellor said that the balance of argument had changed since Ministers had first considered the GGP scheme. The crucial element in the arguments supporting the scheme had been the Department of Energy's assurance that it would not be difficult to obtain private sector finance for it. Over the summer, it had become clear that private sector financing would not be forthcoming except on terms that would be unacceptable to the Government. The prospects of the private sector joining in to finance the project following a public sector launch were not, in his view, at all good. If an integrated line, albeit financed by the public sector, was the only way of obtaining the gas from the Northern Basin, he would be prepared to go along with it: the PSBR arguments, although in his view they favoured the multiple approach, were not decisive. But the multiple approach provided a perfectly satisfactory alternative. It was on this basis that North Sea oil had been developed. This had had the advantage of bringing in the investment as and when it was necessary, and it involved less concentration of risk. It would be better to follow the same approach with Northern Basin gas. The Chief Secretary added that the greater flexibility of the multiple approach, as described by the C.P.R.S., was very important. He was also concerned that our depletion policy would have to be badly distorted in favour of Northern Basin gas if the GGP were to go ahead.

The Secretary of State for Industry said that he had earlier been a supporter of the integrated scheme. But he was now persuaded by the Chancellor's arguments in favour of the multiple approach: in particular, he was impressed by the greater flexibility that the latter would involve. He also believed that, with the multiple approach, there might well be more development of potential gas fields. However, from an industrial standpoint, there would be some substantial disadvantages. Less ethane would be available, and this would put at risk petro-chemical development in the UK. Grangemouth would be at risk, and we would probably lose one potential new petro-chemical complex. There would be criticism from the chemical industry and from the processed plant industry.

/ The Foreign and Commonwealth

The Foreign and Commonwealth Secretary said that the decision on the GGP did not have significant international implications. There would be some embarrassment with the French if it was decided not to go ahead with it because they had been prevented from obtaining seventh round licences in order to conserve gas for the pipeline; but it should be possible to handle this problem. As for the merits of the two approaches, based on his reading of the CPRS report and in particular the points set out in Annex 1, he had concluded that the GGP was preferable to the multiple approach. He was especially impressed by the point that no multiple scheme as such existed, and by the fact that it would mean a significant loss of ethane. Furthermore, it was widely believed that the Government favoured the GGP, and if it was decided not to proceed with it, there would be enormous criticism in the country. He wondered whether it was possible at this late stage to revise the conditions for private sector involvement in it so that it could go ahead on a private financed basis.

Mr. Ibbs said that it should have been possible to arrange matters so that the private sector would support the GGP. It was now apparently too late, but it might be worth making one final effort to bring the private sector in. It was a great pity that the problems of persuading the private sector to participate had not been foreseen earlier. If the only way of proceeding with the GGP was to do so as a public sector project, he believed that it should be dropped in favour of the multiple approach. An integrated pipeline would require conditions necessary to ensure an adequate return on investment - for example, relating to gas prices and depletion policy - that would in any case have damaging side effects; but if it were to be owned and financed by the public sector, it would also involve some very substantial risks. For instance, there was ample evidence that it was more difficult to achieve successful management of public sector than of private sector projects. He disagreed with the Secretary of State's view that it would be easy to privatise the project after launching. If the public sector built the pipeline, the private companies would have no incentive to join in at least until it had been shown to be a commercial success; and this could take a number of years.

In discussion, the following points were made:

- (i) It was pointed out that the BGC Chairman was still insisting on BGC retaining its monopsony position in the northern basin. If this had been broken, then it should not have been difficult to obtain private sector finance for the GGP. Its continuation was likely to put at risk development of the gas fields in the area. Against this, it was argued that it was unlikely that the complete ending of BGC's monopsony would have been sufficient to bring the private sector in. Furthermore, BGC was only able to make a "first offer" for the gas. If their price was unacceptable, the gas producer could always appeal to the Secretary of State to obtain a reasonable price. BGC had every incentive to offer a reasonable price because, if they were to build the GGP, they would want it to be fully utilised; and they would want to avoid unnecessary flaring or sales of gas to Norway.

- (ii) It was suggested that too great a distinction was being made between public sector and private sector financing of the GGP. The banks were still interested in financing the project, and the guarantees they were asking for would only be against contingent liabilities that were unlikely to arise. The scheme would in essence be financed by the private sector. The guarantees that the banks and the companies were looking for were more of a political than a financial nature. Against this, it was pointed out that the banks were not planning to take any equity in the project, and they were only prepared to lend at a higher rate than the Government was able to borrow at, even though their lending would be the equivalent of gilt edged. Their proposals came within the definition of public sector borrowing, and they were expensive.
- (iii) It was argued that it would be electorally disastrous to forgo the GGP. The Government would be abused from every quarter. The public would find it inconceivable that Ministers had turned down such a challenging project. On the other hand, it was suggested that it would be hard to defend a project that the private sector was unwilling to support.
- (iv) As regards the Foreign and Commonwealth Secretary's suggestion that one more attempt should be made to bring the private sector in, it was pointed out that this was what Mr. Liverman had been asked to explore; and his report had concluded that it would not be possible to reach an accommodation with the oil companies in time for the project to go ahead on the required time scale. There was no reason to believe that it was worth reopening this again. Any further delay in reaching a decision would mean continuing uncertainty for the oil companies and would delay the start-up of individual schemes such as those proposed by Mobil.

Summing up, the Prime Minister said she concluded, on balance, that the multiple approach was preferable to a public sector integrated line. It now seemed too late to persuade the private sector to finance an integrated line, and in any case there were serious doubts as to whether they would be prepared to do so except on conditions unacceptable to the Government. Serious doubts had also been expressed as to whether the private sector would be prepared to join in the financing of an integrated line once it had started as a public sector scheme. The multiple approach would therefore almost certainly involve less public money. It would also have a number of other significant advantages over the integrated line. These, in her view, more than outweighed its disadvantages. Accordingly, an announcement should be made that the Government had decided against the GGP, and Mobil should be given the go-ahead for their individual scheme. The Government should also take action as soon as possible to break BGC's monopoly in order to ensure that the gas fields in the northern basin were developed. Further consideration would have to be given to when this could be fitted into the legislative programme.

/The Prime

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- 5 -

The Prime Minister invited the Chancellor, the Secretary of State for Energy, the Secretary of State for Industry and Mr. Fletcher to meet again that afternoon to discuss the terms of a possible statement. This meeting took place and considered a draft prepared by officials; in the event, it was decided that a new draft should be prepared within the Department of Energy for subsequent clearance by other Departments.

I am sending a copy of this letter to John Kerr (HM Treasury), Brian Fall (Foreign and Commonwealth Office), Godfrey Robson (Scottish Office), Ian Ellison (Department of Industry), David Wright (Cabinet Office) and Gerry Spence (CPRS).

*Tim* *Lawson.*

*Tim Lawson.*

J.D. West, Esq.,  
Department of Energy.

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Qa 05668

To: MR LANKESTER

From: J R IBBS

*Primi Minute*

*Mr Ibbs prefer*

*the multiple  
scheme.*

Gas Gathering Pipeline

*IL  
7/9*

1. The CPRS has submitted a paper which was prepared with Department of Energy and Treasury officials. The paper makes no recommendation.
2. My own conclusion is that the integrated pipeline should not go ahead as a public sector project. This is not because I regard the scheme as unsound provided the key conditions are met. However, I do not see its marginal advantages compared with the alternative of multiple private sector pipelines as sufficient to outweigh the undesirability of having a new area of public sector involvement based on a very large project and the associated increase in demand on the PSBR in the years immediately ahead. I would stress that this is a commercial judgement and does not take into account any political factors.
3. I am sending a copy of this minute to Sir Robert Armstrong.

*[Signature]*  
P. J. K. Ibbs

*(Dictated by Mr Ibbs but signed in his absence)*

9 September 1981

CONFIDENTIAL

Prime Minister to see

cc Mr. Wolfson  
Mr. WalkerN.R.G. Mitchell  
Duty Clerk 9/9/81Treasury Chambers, Parliament Street, SW1P 3AG  
01-233 3000

PRIME MINISTER

## GAS GATHERING IN THE NORTH SEA

I have seen Mr. Ibbs' note of 8 September. I should like to emphasise three wider political points arising out of the report by officials which Mr. Ibbs has presented.

Extension of Public Sector Monopoly Power

2. Whatever its advantages, the fundamental objection to proceeding with a public sector integrated line is that it would involve - certainly initially, and probably for some time - a major extension of public sector monopoly power:

(i) An important condition for the integrated line's operation is likely to be the banning of competitive private sector pipeline at least for the next decade.

(ii) The Government will feel that it has to use its depletion powers to improve the profitability of the line by controlling gas development throughout the North Sea in order to provide sufficient throughput e.g. by developing expensive Northern Basin gas ahead of cheaper Southern Basin gas. Perfectly legitimate private sector business decisions would be constrained for the sake of the publicly sponsored integrated line.

(iii) The BGC Chairman has stressed to the CPRS that BGC would not accept financial responsibility for the integrated line if their monopsony is removed. The Department of Energy hope to persuade the Corporation to drop their reservations. But as the CPRS note explains



BGC's wish to retain their monopsony is understandable if they are responsible for the integrated line.

(iv) By the 1990s some 20-25 per cent of UK gas supplies could be coming through the integrated line. At winter peak demand that amount of gas would not be easy to replace from elsewhere in BGC's system. The staff operating this line will thus have enormous industrial muscle. The multiple approach reduces this concentration of industrial power.

In short, a decision to proceed with a public sector integrated line would effectively reinforce BGC's monopsony, which it is our policy to remove and which is at the root of our difficulties in enlisting private sector support. We should have embarked on a public sector planning approach to gathering gas which is in sharp distinction to the very successful private sector solution adopted hitherto to bringing the North Sea oil ashore.

#### Risks and Rewards

3. In view of the private sector's unwillingness to risk their shareholders' money in financing an integrated line, there needs to be strong reasons before the Government commits public money, especially as:

(i) It is agreed that the private sector multiple pipeline system should enable the vast bulk of the £25 bn gas to be brought ashore, and is thus a very good economic prospect.

(ii) 100 per cent public sector financial support for the line does nothing to reduce the degree of financial exposure and risk which the private sector has found so unattractive. The main financial risk in investment in the integrated line is that there will be insufficient gas to go through the line in its early years; and this



is in the hands of the oil companies. Mr. Ibbs' note points out that firm gas developments current amount to 2.3tcf and the scheme needs an estimated 4tcf of gas to ensure its commercial viability.

Thus, the integrated line entails a very large commitment of public funds, and a commitment which is not free of risk. A decision to go that way (with its other attendant disadvantages) does not appear to be justified by the prospect of benefits over and above the benefits obtainable from the multiple scheme where the financial risks lie with the private sector. All our experience over recent years has emphasised the unwisdom of using public credit to support the financing of leviathan projects like the integrated line in conditions of great uncertainty where there is a private sector alternative available.

#### Public Expenditure and the PSBR

4. If it could have been demonstrated that there was an overriding case for the public sector integrated line, I would not have objected to it solely because of the need to keep down the public expenditure totals and the PSBR over the vital next few years of the Medium Term Financial Strategy - though any increase in respect of the pipeline would, if course, mean corresponding economy in other directions. But the necessity for the line is far from overwhelming. In these circumstances it is only prudent to husband the limited public expenditure resources which are available for programmes which cannot be undertaken, or effectively matched, by the private sector.

#### Presentation

5. The presentation of a decision not to proceed with the integrated line would, of course, need careful handling. A possible approach might be:

(i) Further discussion of gas gathering has convinced Ministers that the oil companies will bring the gas ashore. There is no need for a grandiose nationalised industry project financed from the peoples' pockets.





(ii) The highly successful development of the Northern Basin oil fields has been carried out largely by the private sector (with much of the planning being carried out when Mr. Benn was Secretary of State), with virtually no risk to public funds and enormous profit to the country. The Government intends to continue to back this record of success by letting the private sector develop the North Sea gas fields for the benefit of the country as a whole.

6. I am sending copies of this minute to the Secretary of State for Energy, Industry and Scotland and to Mr. Ibbs and Sir Robert Armstrong.

*Jim Rutter*

PP (G.H.)

9 September 1981

*Approved by the Chancellor and signed  
in his absence.*

for en  
showr

British  
TELECOM

dial the number  
r dialling instructions

Telegram for enquiries dial the number  
shown in your dialling instruction



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889113 PO SW G  
73596 PO AB G

5 ABERDEEN 1540 9 25

RT. HON. MRS MARGARET THATCHER  
10 DOWNING STREET  
LONDON SW1

GAS GATHERING VITAL. SOUND NATIONAL INVESTMENT.  
DELAY FATAL DECISION NOW

MALCOLM BRUCE SCOTTISH LIBERAL PARTY

10 SW1

889113 PO SW G  
73596 PO AB G

✓ FSCS



✓ Mr Wolfson  
Mr Walter

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Prime Minister

Qa 05667

To: MR LANKESTER ✓

From: J R IBBS

This is the report  
concerning the GGP with  
the multiple scheme  
which you asked for  
after last week's mtg.

GAS GATHERING PIPELINE

1. As requested at the Prime Minister's meeting on 1 September, I attach a note which has been prepared by the CPRS in collaboration with the Department of Energy and the Treasury. It sets out the case for an integrated gas gathering pipeline that would at least initially be in the public sector compared with the alternative of bringing ashore Northern Basin gas through multiple private sector pipelines.

R  
9/9

2. I am sending copies of this minute and attachment to the Chancellor of the Exchequer, the Secretaries of State for Industry, Energy and Scotland, the Chief Secretary, and to Sir Robert Armstrong.

8 September 1981

Att

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GAS GATHERING PIPELINE

1. Following a meeting with the Prime Minister (Mr Pattison's letter dated 1 September refers), officials were requested to prepare a factual assessment of the prospects of the integrated gas gathering pipeline and the economic case for it; in particular, examining the basis of the Bank of Scotland's interest in providing loan finance. The present paper has been prepared by the CPRS in consultation with Departments to fulfil that remit.
2. Over the last year BP, Mobil and BGC have carried out pre-construction work on the integrated pipeline, committing over £8 million for this purpose. To keep the project on schedule for completion in 1985, major contracts must start to be let before the end of September. By end December ultimate financial commitments under the contracts would be £359 million.
3. The CPRS and officials met with representatives of the Bank of Scotland to explore whether the proposal they have put forward would enable the necessary funding to be provided by the private sector. It was clear however that the Bank of Scotland scheme is designed to provide funds for the integrated project on the security of guarantees given by Government (either directly or indirectly through BGC) that the pipeline will be completed and any gap between the revenue covered by the line and the cost incurred in construction will be made up and the bank loans repaid. In the view of officials, the Bank of Scotland proposals would not take the project outside the public sector, and the loan finance offered would be expensive compared with NLF (Annex 2 gives a fuller account of the Bank of Scotland scheme).
4. It is therefore clear, as Liverman stated in his report, that private sector risk finance will not be forthcoming in time to meet the September deadline, even if changes were made to the present guidelines or concessions offered on gas pricing. The choice therefore before Ministers is either:
  - (i) to launch the integrated line as a publicly financed project with the objective of subsequent privatisation; or
  - (ii) to abandon the integrated project and allow multiple private sector pipelines to be developed as necessary.

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5. In order to make this judgement the CPRS believes Ministers require four pieces of information:

- (i) what are the comparative economics of the integrated and multiple pipeline approaches in terms of national resources (including any benefits that may not be capable of quantification);
- (ii) what conditions attach to each scheme;
- (iii) what are the financial implications of each scheme;
- (iv) what risks are involved.

6. The CPRS has not been directly involved in the issues raised by the alternative approaches to development of gas in the Northern Basin of the North Sea. Differences of view still exist between officials on some of the issues associated with each of the schemes. We have not been able fully to resolve these, but the CPRS believes that this paper, in view of the short time available, is a fair representation of the arguments.

7. The paper starts with an introductory summary of the main arguments, follows this with a more detailed factual description of the integrated and multiple approaches and their characteristics and concludes with an appraisal under each of the headings identified in paragraph 5 above.

SUMMARY OF THE MAIN ARGUMENTS

8. There is no doubt that the vast bulk of the gas reserves in the area that would be served by the proposed pipeline will be developed whether or not the integrated scheme goes ahead. In national terms the economic case for their development is overwhelming. The basic question is whether the earlier commitment and greater call on public funds attached to proceeding with an integrated pipeline is justified by the extra benefits generated and the risks entailed, compared with the alternative of private sector multiple pipelines.

9. The principal benefit of the integrated line is that on the basis of present knowledge of the fields, it offers the better economic return to the nation. However, the timing of the development of individual fields is not within the initiative of Government, but depends on the decisions of individual producers. Their decisions are influenced by many factors,

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including the availability of attractively priced gas contracts, availability and cost of corporate funds and the technical problems of development. One major risk associated with the integrated line is that delay in the development of the fields would mean only partial utilisation in the early years and which would result in a worse commercial return. (There are also the normal risks that go with such a project such as technical difficulties and cost over-runs, but these apply also to multiple developments although the sheer scale of the integrated project might add to these risks.) There are a number of reasons why the oil companies are unwilling to finance the pipeline. One is that they need to be assured that a major risk of low utilisation has been eliminated. Other reasons for the oil companies' non-participation identified in Mr Liverman's report include ownership of existing pipelines, preferential access to pipeline capacity, desire for tax offsets. These represent quite proper commercial negotiating considerations rather than reflecting on the viability of the integrated pipeline itself. To ensure adequate utilisation the oil companies would need reassurance on:

- (i) gas prices;
- (ii) a depletion policy that did not delay or prevent development of the relevant fields;
- (iii) no diversion of gas to competing lines until it was clear that the utilisation of the integrated line would be satisfactory.

The same uncertainties need to be removed if a satisfactory return on a publicly owned pipeline is to be ensured.

10. The multiple approach in addition to having a lower economic return would also only permit partial collection of natural gas liquids for potential use as a feedstock for the UK petrochemical industry. However, it entails different risks. Individual companies will provide pipelines in the light of their own commercial judgement although they would offset the major part of the investment against their tax liabilities. The pipelines would be developed in relation to individual fields at a later date than in the integrated approach; it is therefore arguably more adaptable to changes in the pattern of discoveries and development of gas fields. With the multiple scheme any loss due to under-utilisation falls on the private sector.

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THE TWO SCHEMES

Integrated Approach

11. The integrated approach proposes collecting rich gas (natural gas liquids for use as chemical feedstocks in addition to methane for the gas grid) by means of a 36" diameter pipeline to be laid from Statfjord to St Fergus via a junction in the Thelma area and with a 24" southern leg from this junction to Lomond. This proposal has been the subject of the full feasibility and design study by the Organising Group comprising representatives from Mobil, BP and BGC. The route of the pipeline has been carefully sited to take best advantage of current and future reserves on the basis of existing knowledge. It has also been designed to achieve bulking of natural gas liquids for potential petrochemical use. The total cost in 1981 money is an estimated £1.5 billion of which some £875 million (55 per cent) is offshore, the remainder being onshore facilities at St Fergus and Nigg.

12. A characteristic of the integrated line is that it involves earlier financial commitments and investment for the future. The line is being designed to be capable of transporting a minimum of 11 tcf of gas over its lifetime; firm developments currently amount to 2.3 tcf and the scheme needs an estimated 4 tcf of gas to ensure its commercial viability. The Department of Energy expect that a further 3.4 tcf will come forward over the next two years. The whole or greater part of the integrated line is to be laid at the outset to take advantage of the associated gas now available from oil fields (see paragraph 15 on possible project break-points). However, the overall economics of line depend only partially on associated gas, two-thirds of the throughpnt will come from subsequent development of condensate and unassociated gas fields along the route of the line.

13. The financial return in the early years from the integrated line depends on enough gas being developed and transported during that period. For this reason the following conditions need to be fulfilled if it is to show a satisfactory commercial return (this would be true irrespective of whether the pipeline was financed publicly or privately):

- gas from fields in the vicinity is fed exclusively into the integrated pipeline and not into rival pipelines;
- gas field developments in the Northern Basin are not delayed by depletion policy;

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- if BGC's monopsony were removed the development of some cheaper cost Southern Basin gas might have to be delayed to make room for Northern gas depending on the total volume of gas production, the size of the UK market and whether or not exports were permitted.

All these points are fully within the Secretary of State for Energy's control under existing powers. It should be added, of course, that once there was satisfactory utilisation of the line there would be no reason to block further pipelines or constrain depletion policy decisions. Once that stage was reached, probably by the end of this decade, there would be competition between pipelines; at present, because of the different areas they serve, the existing pipelines are each in an effective monopoly position.

14. A particular problem that might apply in the case of publicly financing the integrated line is whether BGC would accept the total risks associated with the pipeline if its monopsony were relaxed. As long as BGC is a monopoly purchaser of gas, it is willing to accept the risks. When the CPRS saw Sir Denis Rooke in the preparation of its previous report (Mr Ibbs's minute to Mr Lankester dated 31 July), the BGC Chairman was adamant that BGC would not accept the total risks if its monopsony were removed. The Department of Energy believe that this may be a negotiating stance and hope that it would be possible to persuade the Corporation to set aside its reservations. However, BGC's attitude is understandable and in principle is the same as the one the oil companies have used in laying down their conditions for participation: the oil companies will not accept a share of the risks involved in the integrated pipeline unless they receive some reassurance on price and therefore the pace of gas development; BGC will accept all the risks as long as it has control over prices and availability. The integrated pipeline predicates a commitment to produce a minimum quantity of higher cost Northern Basin gas in preference to cheaper Southern Basin gas and, if BGC's monopsony were removed, the Corporation may not be willing to shoulder the commercial risk entailed unless it received satisfactory depletion assurances from the Department of Energy.

15. The integrated scheme does provide some flexibility in that the whole of £1.5 billion capital expenditure need not be committed at the outset. Offshore, no commitment is yet needed on the southern section of the line from the T junction to Lomond; onshore, an additional gas



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processing module at St Fergus could be delayed. These break-points in capital expenditure mean that a decision to launch the integrated scheme would represent a definite financial commitment of £1180 million, corresponding to about 80 per cent of the total estimated project cost. The contracts would, of course, contain the usual clauses permitting cancellation at a cost in the event of circumstances changing.

The Multiple Approach

16. The alternative scheme examined by Department of Energy and Treasury officials involves multiple development of the 16 fields supplying the integrated line. Because we cannot predict the state of knowledge at the time they are built, it is not possible to predict precisely the configuration or timing of such multiple pipelines. For the purposes of comparison with the integrated scheme Department of Energy and Treasury officials have agreed an overall multiple scheme as being a fair representation of the best outcome. In this scheme Beryl and some other fields would bring their gas ashore through a smaller diameter dedicated pipeline (Mobil's original proposal) whilst other fields construct long laterals connecting into the existing Flags and Frigg trunk pipeline systems.

It is assumed that gas from the southern field Lomond is collected by a subsequent private sector gas gathering line at a later date and at a cost equal to that of this part of the integrated system.

17. Because it makes use of existing pipelines the estimated capital cost of the best multiple alternative at £1.2 billion is lower than the integrated line but the annual running costs would be higher. The capital costs would be spread over a much longer period because expenditure would be made only as fields were developed. It follows that gas supplies from the Northern Basin would be lower in the early years in comparison with the integrated scheme.

18. It should however be emphasised that whereas the integrated scheme has been thoroughly costed by BP, Mobil and British Gas in detailed engineering and design studies, the multiple approach costings are very much a broad-brush estimate. It assumes that the configuration of pipelines and the timing of field developments takes place in such a way as to minimise the pipelines involved. The eventual reality may be different; the tax incentives or disincentives in future and the scope for charging high tariffs on existing pipelines may be strong distorting forces.

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19. The multiple approach involves a later commitment of capital than in the integrated project and gas fields are developed as and when market forces demand and as knowledge of gas reserves improve; the economics are not dependent on the conditions in paragraph 13 being observed. In this sense it is more flexible, albeit that the two major gas collecting pipelines in the scheme (Flags and Frigg) are already in place.

20. In the multiple approach to the extent that ethane or LPG had to be routed through the Frigg system those materials would not be landed in sufficient quantities to justify economically their separation from the stream sold to British Gas (Department of Energy officials assume some 9 of the 16 known fields would be so routed). This would reduce the availability of gas liquids for use as chemical feedstock. This, in combination with a more extended profile of gas production in the multiple scenario could reduce the availability of ethane for petrochemical plants by 60 per cent. Depending on the state of the market, this could mean anything from forgoing the opportunity of an additional ethylene cracker in the UK in the 1990s to not preserving one of our existing complexes.

COMPARISON BETWEEN THE APPROACHES

Economic Appraisal

21. Department of Energy and Treasury officials have carried out an economic comparison between the two approaches to Northern Basin gas development. This has already been submitted to Ministers. It assumed that both schemes collect the full 11 tcf in 16 fields with sizeable gas reserves taken into account by the Organising Group (BP estimate that ultimate reserves may exceed 20 tcf). This demonstrated conclusively that in view of the huge disparity between the total net value of reserves and the capital cost of development (a) there is an overwhelming case for the development of a line or lines to bring those resources ashore; and (b) this conclusion will remain robust against realistic sensitivities in the key economic parameters - variations in the cost of the schemes, variations in reserves, uncertainty as to future energy prices, etc.

22. Furthermore, in national terms this analysis showed a real net present value in favour of the integrated scheme of at least £50 million discounted at 5 per cent and £300 million discounted at 10 per cent. The

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integrated pipeline, although more expensive in capital terms, realises a higher value for the gas by full separation of LPG and has lower operating costs.

22. This economic advantage in favour of the integrated line would be further advanced if the configuration of pipelines in the multiple approach turned out in reality to be less favourable than assumed, and if gas prices rose more slowly than assumed (the value of gas is assumed to rise by almost threefold in real terms from 1980 to 2000). Sensitivities were quantified in the joint Department of Energy and Treasury economic comparison.

23. In addition to this quantified advantage the integrated approach has further potential benefits that are not quantifiable:

(i) it permits full separation of ethane as a potential feedstock for the UK petrochemical industry;

(ii) the absence of an integrated line would make it impossible to obtain Norwegian Statfjord gas at distress prices for a few years if, as is quite likely, the Norwegian pipeline encountered delays;

(iii) towards the end of the century an integrated pipeline would offer better access for obtaining gas supplies from Norwegian waters;

(iv) the integrated scheme offers larger and earlier orders for UK contractors;

(v) in the integrated approach there will be less leakage of money to existing (foreign) pipeline owners in the form of monopoly tariffs, but it is difficult to quantify the amounts involved;

(vi) it offers better insurance against the possibility of distress sales of associated gas to Norway where there is no appropriate UK pipeline.

24. The integrated approach also brings gas from the Northern Basin ashore sooner than in the multiple case, but no value or penalty in national terms has been put on this in the economic calculation other than through the assumption on steadily increasing gas prices.

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Comparison of the Practical Implications of the Alternatives

25. As described previously (paragraph 13) to ensure the commercial viability of the integrated line gas development policy throughout the North Sea could become constrained by the need to provide the early throughput for the line. Rival pipelines would need to be banned and it could be necessary to restrain production of the cheaper cost Southern Basin fields. In contrast, since most of the investment required for the multiple scheme would not be committed until later than that entailed by the integrated line, decisions concerning alternative schemes could be taken in the light of later information concerning depletion policy and ending of BGC's monopsony as well as prospective gas supplies, demand and prices.

26. The Table below illustrates the level of expenditure involved in the integrated pipeline and multiple approach:

	<u>Capital Expenditure at January 1981 Prices £m.</u>					
	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1985</u>	<u>Later Years</u>
Integrated Pipeline	60	230	470	450	180	150
Multiple Alternative				300	350	550

Note The timing of pipeline expenditure in the multiple alternative is uncertain.

27. The effect of the PSBR is extremely complex, involving a combination of capital expenditure under the integrated approach and tax reliefs under both approaches. The uncertainties inevitably increase as one looks further ahead. Looking at the effect of pipeline expenditure over the next 5 years, it seems likely that -

- (i) an integrated line which remained in the public sector would involve a higher PSBR charge than multiple schemes;
- (ii) but an integrated line which was privatised could offer a lower PSBR charge than multiple developments. \*However, early privatisation cannot be guaranteed. The Treasury believes that it is a prudent assumption to make that control is unlikely to pass to private shareholders for a number of years.

\* While the pipeline company remains in the public sector, proceeds from the sale of shares would be classified as public sector borrowing and would not reduce public expenditure or the PSBR. Only when control passed to the private sector, would proceeds from the sales of the residual BGC holding of shares reduce public expenditure and the PSBR.

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Looking to the longer term, an integrated line which remains in the public sector will yield positive PSBR contributions from tariff income.

28. Thus the key decision Ministers are required to make is whether the greater economic benefits offered by the integrated pipeline are justified by the incremental capital expenditure, greater burden on the PSBR in the early years and possible constraints on North Sea gas development policy during the 1980s. In making this judgement consideration must also be given to the differing risks involved in the two schemes. Some of the major risks to be compared are:

(i) by definition the financial risks of multiple pipeline approach falls to the private sector, albeit that tax offsets mean that the bulk of the burden is likely to be passed on to the Exchequer. However, in the integrated scheme the public sector would be directly exposed to all the financial risks until the pipeline company was successfully privatised. The risk would be larger (£1.5 billion compared with £1.2 billion) and would arise sooner;

(ii) an extremely large project like the integrated pipeline inevitably concentrates the risk of cost over-runs; against this all the figures for the multiple scheme are very broad-brush and approximate;

(iii) there is a risk that the multiple approach might not collect all the available gas. Any shortfall could carry with it a significant penalty in national terms. Department of Energy officials argue that in the absence of readily available collection facilities smaller accumulations of gas are unlikely to be developed and one could not rely on companies' decisions to achieve the collection of all the gas that could economically be recovered. On the other hand, the integrated line has been designed on the basis of existing knowledge and the multiple approach, with its later capital expenditure, can arguably better profit from future knowledge.

SUMMARY

29. As an aid to Ministerial discussion the major factors are summarised in tabular form in Annex 1.

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ANNEX 1

SUMMARY

A. Description of projects and conditions necessary for their success:

	<u>Integrated</u>	<u>Multiple</u>
Project	Construction of a 36" pipe from Statfjord to St Fergus via Thelma, with a 24" southern leg from Thelma to Lomond.	Construction of a small diameter dedicated pipe from Beryl, and long laterals to the existing FLAGS and Frigg Lines. Lomond gas to be landed later through a future Southern Basin gas gathering line.
Project Definition	Detailed	Outline only.
Gas separation capability	Facilities for bulking NGLs onshore.	Limited facilities for separating NGLs.
Investment Start Date	September 1981	Probably 1983-4.
Flexibility	Very limited, about 20% of the investment could be delayed until late 1980s (Southern leg to Lomond, gas processing module at St Fergus, onshore investment elsewhere in Scotland).	The FLAGS and Frigg lines already exist. Additional capital expenditure will be committed in stages.

	<u>Integrated</u>	<u>Multiple</u>
Conditions necessary to ensure planned return on investment	1. No rival pipelines.	1. PRT Tax relief for pipelines continues.
	2. May require imposing equivalent depletion controls if BGC's monopsony is removed.	
	3. No delay in development of N Basin reserves, to ensure adequate throughput.	

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B. Economic Factors\*

	<u>Integrated</u>	<u>Multiple</u>
Capital cost	£1.5bn	£1.2bn
Operating cost per year	£50m	uncertain, but more than £50m
Reserves of gas available to line	11 tcf identified (maximum estimate 21 tcf)	11 tcf identified (maximum estimate 21 tcf)
Value of gas landed at full opportunity cost	£25bn	£25bn maximum, but perhaps £23bn or less
Quantity of NGLs captured	All available	much less, about 40% of available ethane
Field development cost	about £3bn	about £3bn
Comparison in national terms (but without risks) shows NPV in favour of integrated scheme		
Capital Expenditure Profile* (£m)		
1981	60	-
1982	230	-
1983	470	-
1984	450	300
1985	180	350
Later Years	150	550

\*January 1981 prices

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C. Risks (including factors identified in A as conditions necessary for success).

	<u>Integrated</u>	<u>Multiple</u>
Premature investment, siting and sizing	more vulnerable	
Technical difficulties and cost overruns	more concentrated risk	
Failure to capture full gas reserves		more vulnerable
Risk that producers might not develop fields to use the pipeline	more vulnerable	
Risk of flaring		more vulnerable
Potential loss of UK gas to Norway and subsequently Norwegian gas to UK		more vulnerable
Loss of NGLs and reduced opportunity for bulking for petrochemical use		more vulnerable (possible 60% lost) might mean forgoing a new cracker; or loss of an existing complex
Opportunity for early placing of contracts with UK companies		less opportunity
Speed of subsequent privatisation	uncertain	fully private ab inito

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BANK OF SCOTLAND LOAN FINANCE  
PROPOSALS

Officials have discussed with representatives of the Bank of Scotland their proposals for providing loan finance for the gas gathering pipeline project.

The Bank Study Group includes Barclays, Citibank, Lloyds, Morgan Guaranty and National Westminster and is chaired by the Bank of Scotland. The Group was originally asked to put forward proposals for interim finance of £700m but having reviewed the project they suggested that project financing on the basis of estimated ultimate cost and for a more extended period should be considered.

Bank of Scotland Scheme

The essential features of their scheme are that the banks would lend money to be repaid from the cash flow generated by the completed pipeline. The money would be secured against pipeline fees attributable to "bankable" reserves of gas, ie. reserves for which Annex B development approval had been given. As Annex B approvals were granted, the amount of bankable gas would increase and so in turn would the amount of money available from the banks. The banks would not, however, enter into the loan unless they were satisfied from the beginning that sufficient funds would be forthcoming to complete the project. At present there is not enough bankable gas to cover the project's estimated cost. The banks would therefore require a guarantor to meet any deficiency that might arise; if expenditure on the pipeline ever exceeded the value of bankable gas, the deficiency guarantee would be called. The guarantor would then have to decide whether to stop the project and pay bank the loans, to put up the money necessary to allow the project to continue or to arrange for more bankable gas to be approved.

Benefits

The purported attractions of such a scheme are first, that money could be borrowed against gas for which development approval had been given, rather than having to wait until a throughput contract had been signed. Secondly,

provided the pipeline project is viable, no actual liability would arise in the long term because the value of pipeline fees attributable to the bankable gas would greatly exceed the construction cost of the pipeline. Sufficient volumes of gas would however have to come forward and, at least until enough gas was contracted to pass through the integrated line for the project to become viable, no competing pipelines could be allowed. Thirdly, the pipeline construction company could be a small company with only nominal capital. The running of the company would be contracted to an organisation with the appropriate experience. Equity in the company could be sold at a later date, perhaps in 2 or 3 years time, when throughput contracts had been signed and the net worth could be more accurately assessed.

#### Disadvantages

The repayment of the loan finance is intended to come from the cash flow generated by the pipeline, that is, by the tariffs earned from gas passing through the line. The "value of bankable gas" referred to by banks would be based only on fields that had been given Annex B approval (currently 2.3 tcf of the total 11 tcf), and would be derived for each field, mainly from the reserves, production profile and transmission charge that could be made. Although the Bank of Scotland representatives emphasised that they could not be expected to be specific before the details of any loan had been sorted out, it appeared that they had in mind an interest rate of around  $\frac{3}{4}$  -  $1\frac{1}{2}\%$  above LIBOR. This is likely to be expensive compared with not only NLF finance but also the rate at which nationalised industries borrow from the banks. The amount of money to be raised is large but the Bank believed it would be possible to raise it from a worldwide syndicate of banks. Fees would be charged for the placement of loans with these banks.

The most serious limitations of the Bank's proposals are, however, the need for a deficiency guarantee (amounting in practice to a completion guarantee) and the problem of responsibility for the pipeline company. Ultimate responsibility for it would lie with the deficiency guarantor who would be liable for any gap between the value of bankable gas and what was required by the company for building the line. The Bank emphasised that the deficiency guarantor would have to be a credible and creditworthy source; they suggested the Treasury or BGC.

Conclusions

This scheme is designed to provide funds for the project on the security of guarantees given by the Government, either directly or indirectly through BGC, that the pipeline will be completed and that any gap between the revenue earned by the line and the cost incurred in building it will be made up and the bank loans repaid. If BGC or the Government were the deficiency guarantor, the Bank of Scotland proposals would not take the project outside public sector and the loan finance they offer would be expensive.

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7 September 1981

I am writing on behalf of the Prime Minister to acknowledge your letter of 4 September with which you enclosed a copy of the telegram which had earlier been sent concerning the gas gathering pipeline. The letter has been drawn to the Prime Minister's attention.

T. B. LANKESTER

James M. Dunlop, Esq., C.B.E.

1/10



FIFE REGIONAL COUNCIL

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JAMES M. DUNLOP, C.B.E., *Chief Executive*

The Rt. Hon. Margaret Thatcher, M.P.,  
Prime Minister,  
10 Downing Street,  
LONDON, W.1.

*mt*

Your Ref.

Our Ref. CE/JNP/

If telephoning or calling please ask for

Mr. Dunlop.

Date 4th September, 1981.

Dear Prime Minister,

Gas Gathering Pipeline System.

I enclose a copy of the telegram which was sent to you today.  
The Local Authorities and Members of Parliament hope that it will be possible for the Cabinet to arrive at an early decision on this most important matter.

Yours sincerely,

*James M. Dunlop*  
Chief Executive.

Encl.

*Ann Thistle*

*I have  
acknowledged the  
attached telegram.*

*R.*

*9/7/81*

TELEGRAM.

The Rt. Hon. Margaret Thatcher, M.P.,  
Prime Minister,  
10 Downing Street,  
LONDON, W.1.

Gas Gathering Pipeline System.

According to Press reports, the Cabinet are discussing the North Sea Gas Gathering system.

You will be aware of the developments by Shell and Esso at Mossmorran and Braefoot Bay in Fife. The under-signed, who are representative of the Local Authorities in Fife and all the Fife Members of Parliament wish to stress the importance of the Gas Gathering system to the national economy and the particular importance the project has for this Region. The Mossmorran/Braefoot Bay developments have an important part to play in assisting the Government in achieving their objectives as expeditiously and economically as possible. The Gas Gathering system is essential for the long-term viability of these projects in Fife and will also ensure an economic return on public expenditure already committed in connection with these projects. It will create a welcome increase in employment opportunities in British industry.

We, the under-signed, accordingly consider it vital that the Government authorise an early commencement of the Gas Gathering Pipeline System.

(Signed)

ROBERT GOUGH, CONVENER,  
FIFE REGIONAL COUNCIL.

LES WOOD, PROVOST,  
DUNFERMLINE DISTRICT COUNCIL.

ROBERT KING, CONVENER,  
KIRKCALDY DISTRICT COUNCIL.

DICK DOUGLAS, M.P. for DUNFERMLINE.

HARRY GOURLAY, M.P. for KIRKCALDY.

W. W. HAMILTON, M.P. for CENTRAL  
FIFE.

BARRY HENDERSON, M.P. for EAST  
FIFE.

010  
RESIDENT: EDMUND VESTEY

Telephone 01-283 2922

115  
GENERAL COUNCIL OF BRITISH SHIPPING

30-32 ST. MARY AXE

L4  
LONDON, EC3A 8ET

3rd September, 1981

The Rt. Hon. Margaret Thatcher, MP.,  
Prime Minister,  
10, Downing Street,  
London, S.W.1.

Dear Prime Minister.

As compared with other industries, shipping has not a major interest in the proposed North Sea gas-gathering project. But I would like you to know that British offshore supply, diving, anchor handling and pipe-carrying vessels, which have had a hard time until recently, would greatly welcome the increased business and employment opportunities inherent in the scheme.

I am copying this letter to the Secretaries of State for Energy and Trade.

Yours sincerely  
Edmund Vestey.





10 DOWNING STREET

- 1 Mr Whitby <sup>sub 21x</sup>  
2 Mr Lankester (o.v.)

The attached. I have now  
set up a further meeting on  
the gas gathering pipeline at  
1100 on 10 September. Howell  
(+ Gray), Howe, Joseph, and  
Fletcher (Sutton's office) will attend  
as well as 1663, Walters, and  
officials.

WJH

2/9

MR. LANKESTER o.r.

cc: Mr. Rickett

This week's gas-gathering pipeline meeting was not a success. The Prime Minister had a long talk with the Chancellor over the weekend and, after consulting DT, concluded that she had not been provided with anything approaching the quality of information and analysis required to reach a decision about committing £1.5 billion.

As a result, she asked that the officials present (basically Robin Ibbs, Nigel Wicks, Alan Walters and Philip Jones) should prepare a factual assessment of the prospects for the project, including an assessment of its economic viability. This, together with any covering comments from the Ministers involved, is to be the basis of a further meeting which Willie Rickett will set up for 1100 hours on Thursday 10 September. The Ministers involved will be those who came to the 1 September meeting, or their Cabinet colleagues if then available, plus an Industry Minister. Ministers are free to bring an official.

1 September 1981

MA



WFO

10 DOWNING STREET

THE PRIME MINISTER

7 September 1981

*Dear Mr. Vestey,*

Thank you for your letter of 3 September about the interest of the snipping industry in the gas gathering pipeline project. I have taken note of what you say, and my colleagues and I will of course bear it in mind when we give further consideration to the project.

*Yours sincerely  
Margaret Thatcher*

Edmund Vestey, Esq.

—

*JUP*

PRIME MINISTER

HISTORY OF GAS GATHERING PIPELINE PROJECT

1. This began with a letter dated 2 July 1979 from David Howell to George Younger.

"We are now increasingly confident that UK gas reserves would justify a new pipeline; indeed that a new line will be necessary if we are to avoid flaring substantial quantities of gas in the second half of the coming decade."

It continued later:

"The final impetus for a new look arose when Mobil indicated that it was considering an application for authorisation to construct a pipeline to transport gas from its Beryl field to the UK".

It is somewhat strange that our present situation arises from a private sector application to build a private sector pipeline!

2. A year later on 10 June 1980 Robert Armstrong minuted you with regard to the gas gathering line discussion at E.

"It is generally agreed that the economic case is robust and that the scheme compares well with the alternative of collecting gas through existing pipelines and flaring other gas or leaving it in the ground. It is thought that the pipeline would also stimulate development of further oil and gas reserves. The recommendations are judged to be technically sound."

At this point the idea of a central gas gathering line has so taken over that there is no discussion of the alternative of several lines. Indeed it is assumed that without this pipeline other gas will have to be flared or left in the ground. Somewhere in the course of this year the multi-line solution has been completely lost sight of.

3. The E discussion on 11 June 1980:

"The Prime Minister, summing up the discussion, said that it was agreed that the Government should strongly encourage construction of the proposed pipeline with a view to its completion by 1984/5."

The proposed pipeline of course was going to be constructed and operated by a private sector company, etc., and

"the organising group .... should be left in no doubt that the Government was not guaranteeing the loan financing."

4. Hansard, 19 June 1980:

David Howell:

"At today's high energy prices.....our offshore gas reserves represent an increasingly precious national resource. The Government are determined to make the most of that asset and to eliminate uneconomic waste of gas by flaring....we consider however that a pipeline system along the general lines recommended would be in the national interest. The integrated gas gathering concept would, through its economies of scale, both allow the development of smaller gas accumulations and facilitate the most economic collection of larger gas deposits. It should also reduce wasteful offshore flaring and encourage further exploration within its catchment area..... the Government consider it important that a gas gathering system should be constructed as quickly as possible."

We are here unequivocally supporting the centralised concept putting it forward in the national interest as leading to greater recovery of gas. This quotation will be extremely damaging should the central concept be lost. [In Guardian Sept 8 '7]

5. Eldon Griffiths to Prime Minister, 30 October 1980:  
"The high hopes of early completion of the big new gas line seem likely to founder on the Gas Council's monopoly."

This is the first significant mention of the inherent contradiction between wanting private risk finance of a pipeline and having a monopoly state buyer already in place.

6. In your reply to Eldon Griffiths, 8 December 1980: You "agree .....on the importance of this project and the need to avoid delay." and go on to say you believe his fears are unfounded and "that good progress is in fact being made."

You say later:

"There now appear to be reasonable prospects, on banking advice, of raising funds for at least the first two or three years of construction ahead of the firm purchase/sales agreements which your information had suggested was a prerequisite of financing."

"In summary, significant progress has been made to date and the picture is far more promising than you may have been led to believe".

7. A note from Department of Energy to you via Tim Lankester dated 3 April 1981:

"For the critical early years this result (satisfactory gas availability) depends on including gas from North Alwyn, whose licensees (Total and Elf) are now preparing to seek development approval. Total and Elf wish to put North Alwyn gas into their Frigg pipelines. ....we are pressing them to commit North Alwyn gas to the gas gathering line; meanwhile, we are holding back award of Seventh Round licences for which they had applied."

/ The ugly

The ugly head of a private sector solution has again been raised and is being driven below the surface by the Department of Energy! Later the note says

"It is vital that the project should not be delayed and we must now face the fact that sufficient (financial) support may not be mustered in time. To bridge this "time gap" there is probably no alternative to some kind of limited - and reducing - guarantee or security being given either by HMG or preferably British Gas Corporation."

The requirement for Government guarantees has now been brought into the open and within six months the limited nature of the guarantees will of course disappear.

8. Letter from David Howell to Chancellor of 16 April 1981:  
"We cannot afford to allow the project to falter. Any delay would, in my judgement, cause the present scheme to collapse with serious consequences for gas supplies".

So the scheme must go ahead at all costs; there appear to be no alternatives.

9. David Howell to Chancellor of 29 June 1981:  
".....project remains highly economic. There is an overwhelming case for a gas gathering system.... Even the most favourable pattern of piecemeal developments would certainly be less economic than the integrated scheme and could be seriously worse to the extent that it failed to collect all the gas reserves for which the integrated scheme is designed."  
"We therefore need to decide well before the end of July where the finance is coming from if we are not to lose the chance of building the most economic and nationally favourable gas gathering scheme. The only feasible way now to keep the

/ integrated

integrated scheme going is for BGC to bear the risks initially."

10. David Howell to Prime Minister of 26 August 1981:  
"The alternative of abandoning the scheme would, I am convinced, be both economically wrong and particularly disastrous."

POLITICALLY

Whilst Energy are now totally convinced that this is the only worthwhile scheme, the most fascinating part of John Liverman's report was the weight of oil company opinion against an integrated scheme. Nowhere in the entire correspondence do Energy raise the disadvantages of a single scheme - in terms of flexibility, of the eggs in one basket, liability to industrial disruption, etc.

Alan Walters would of course argue that the oil companies spend their lives negotiating with one another and are liable to find a better scheme, recover more gas, at lower cost, etc. yet the assumption throughout all the papers is that there is no alternative case.

7 September 1981



CONFIDENTIAL



file

10 DOWNING STREET

From the Private Secretary

1 September 1981

BF 9.9.81

Dear Julian

As you know, the Prime Minister held a meeting this morning to review the position on the gas gathering pipeline, in the light of the Liverman Report submitted under cover of your Secretary of State's minute of 26 August. Mr. Gray, accompanied by Mr. Jones, was present. Others present included the Chancellor, the Chief Secretary and Mr. Wicks, Mr. Fletcher with Mr. McClellan, Mr. Ibbs and Mr. Walters.

The Prime Minister said that the information which had been submitted to her did not provide an adequate basis on which to reach a decision about investing the sums of public money which would now be required to go ahead with the pipeline. The economic viability of the project was not demonstrated in the papers submitted to her. This was dependent on the future pricing policies for gas and in particular on the Government's decisions about the British Gas Corporation's monopsony. Most of the pipeline's capacity would be used only if there were suitable incentives, that is to say high enough contract prices, offered to the oil companies. Furthermore, it was not clear how the integrated pipeline option would affect plans by private operators to operate their own pipelines. While she was sure that these questions could be answered, Ministers would have to consider them before reaching decisions.

In discussion, it was pointed out that the three most recent studies of the project saw the integrated pipeline project as in the national interest. If it did not go ahead, there would certainly be some loss of gas. The Government was widely believed to be committed to the concept, although to a substantially privately funded project, and there would be a major presentational problem in explaining any decision to back out at this stage. The British Gas Corporation recognised the importance of pricing policy in the development of some of the major gas fields, and greater flexibility had already been introduced into their approach. Total and Elf were now coming round to the idea of putting their gas into the pipeline.

/On the other hand,

6

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On the other hand, it was pointed out that the oil companies would have little incentive to join in financing at a later stage on the basis now proposed. Many of them would themselves prefer the flexibility of independent pipelines. On the most favourable position assumptions, no more than 35% of the equity finance would come from the private sector. Whilst the Bank of Scotland was apparently ready to provide loan finance of around £700 million, this would require a Government completion guarantee. In the present state of the petro-chemicals market, the definite advantages of the project were limited to some increase, but not for two years, in overall gas supplies and a bulk supply of low-cost ethane for existing users. The British Gas Corporation would only be prepared to go ahead with the project with a guarantee that the monopsony would remain.

The Prime Minister recognised that the Government would have to decide whether to give the go ahead shortly, so that alternative private sector schemes would not be further stalled. Ministers therefore needed to be provided with a factual assessment of the prospects of the project and the economic case for it. She asked that this should be prepared by the officials present at the meeting, consulting others as necessary. This should, in particular, look into the basis of the Bank of Scotland's interest in providing loan finance. Ministers would need to meet again in the next week to reach a conclusion.

I am sending copies of this letter to John Kerr and Terry Matthews (H.M. Treasury), John Wilson (Scottish Office), Gerry Spence (CPRS) and David Wright (Cabinet Office).

*Yours ever*

*Mike Paterson*

J.D. West, Esq.,  
Department of Energy.

PRIME MINISTER

Gas Gathering Pipeline: UK Orders

If the pipeline were to go ahead on the lines envisaged by BGC, British Steel are now thought to have a very good chance of getting the bulk of the steel orders, and possibly the entire order. The value of the orders involved would depend on final technical decisions. The off-shore pipeline is likely to be worth something in the region of £150 million at 1981 prices and the on-shore pipe would be worth about £50 million, with additional expenditure on laying.

British Steel's competitive position has improved significantly over the last 12 months, so that their prospects are now much better. If they were to be involved, the pipe would be produced in their Hartlepool plant, with deliveries falling due between mid-1982 and mid-1984.

On the process plant side, BGC estimate that something in the range £150-200 million would be spent on process plant for St. Fergus. There is much greater uncertainty about how much of this would come to UK companies.

*MAD*

1 September 1981



SCOTTISH OFFICE  
WHITEHALL, LONDON SW1A 2AU

CONFIDENTIAL

PRIME MINISTER

GAS GATHERING IN THE NORTH SEA

I understand that you propose to discuss with colleagues on 1 September how we are to proceed with the proposed gas gathering scheme. I regret that I will not be able to attend but Alex Fletcher will do so and will cover any specific aspects which emerge from the Report submitted by Mr Liverman. I would like, however, to underline the importance I attach to the project.

The concept of an offshore gas gathering system goes back many years but it was the BGC/Mobil study in 1979 which gave the necessary fillip towards realisation. The Government's endorsement of its recommendations attracted widespread support from all sectors of industry and we have been able to cite our promotion of it as evidence of our intention to obtain maximum economic benefit for the nation from North Sea oil and gas developments.

A crucial feature of this scheme is that, despite other uncertainties, the economic benefits are not in doubt. As the CPRS study made clear, gas and gas liquids valued at £25 billion will be secured in return for an investment of only a fraction of that amount. There is no alternative available on which we can rely with any confidence likely to yield so high a return to the nation. Indeed it is evident from all the appraisals that have been carried out, including one undertaken recently jointly by the Treasury and the Department of Energy, that the gas gathering project would produce a level of return which would justify it being accorded a high priority as a capital project.

And there is much more at stake than the yield to the nation in terms of the financial value of the scheme. If we failed to proceed with the project, doubt would be cast both at home and abroad (with unfavourable comparisons being made with the Norwegian approach) on our ability to manage our reserves efficiently. There would also be a major loss of potential benefit to British industry through the work which the scheme would provide. Again, gas would necessarily be forfeited and one of the major industrial benefits of the current gas gathering proposal - the scope offered for the aggregation of large quantities of gas liquids - would be very seriously jeopardised. This last aspect would be a particular loss to Scotland (and potentially also to Tees-side) in reducing the scope for using the feedstock to secure existing petrochemical operations and to provide the basis for new developments such as those proposed by Dr Hammer of Occidental in Grampian Region and by Dow for the Cromarty Firth.

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We have then a project whose benefit to the nation far outweighs the projected costs, and yet the private sector is unwilling to invest in it at the outset. This was perhaps inevitable given our concern to ensure that the pipeline company did not exploit the monopolistic position in which it would find itself with the result that the investors in the pipeline do not see the prospect of substantial economic gain to the nation reflected in sufficient benefit to themselves. But we must secure private participation, and I think this can now be done only by some adjustment of the original guidelines. I appreciate that in doing so and in authorising the backing necessary to get the scheme launched in time there will be PSBR implications but I believe it would be a great mistake to allow a scheme of such importance to founder because we find ourselves confronted by a problem in setting out the mechanics of its financing. The only alternative of multiple development offshore would not only be much inferior in terms of national benefit in my opinion but would also result in a significant short run increase in the PSBR through the reduction that would occur in Government receipts from offshore taxation.

I am copying this minute to Geoffrey Howe and David Howell. I have also now seen David Howell's minute to you of 26 August and am also therefore copying this to Peter Carrington and Keith Joseph, and to Sir Robert Armstrong and Mr Ibbs.

*J.S. Wilson*

(Approved by the Secretary of State  
and signed in his absence.)

29 AUGUST 1981

CONFIDENTIAL



cc A Walter  
A Duguid

PM/81/41

PRIME MINISTER

Gas Gathering Pipeline

1. In his letter of 26 August David Howell argues that we should now authorise British Gas to underwrite the initial financing of this major project, despite the PSBR and other disadvantages.
2. I find David Howell's arguments entirely convincing. The proposed gas gathering pipeline is perhaps the largest single economic project with which this Government has been associated. The calculation of its longterm profitability, as well as its contribution to our national energy policy, is generally recognised and has been endorsed, I understand, by the recent CPRS study. Private companies are, for understandable if narrow reasons, unwilling to take the initial risks. This is thus pre-eminently one of those cases where Government must take a hand.
3. There are also some important political considerations. Over the past two years the Government has invested a good deal of capital, both at home and abroad, in its advocacy of this project. To abandon it could only damage confidence in the Government's determination to pursue its objectives consistently and Britain's ability to manage large scale major projects successfully.

/4. The



4. The gas gathering pipeline could give us the capacity to export gas to the Continent. The economic arguments remain to be worked out. But a pipeline network, involving the Norwegians as well, would be a contribution to European energy security, about which President Reagan expressed his concern at the Ottawa Summit. If we abandon the pipeline that option would be foreclosed.

5. Earlier this year I reluctantly agreed that licences for two French companies wishing to explore in the North Sea should be withheld until they had agreed to put their gas into our pipeline. They are now beginning to move. And we have worked hard to persuade the Norwegians to put some of their gas through our pipeline despite their preference for their own rival project. Though for the time being the Norwegian decision has gone the wrong way I am not sure that that is the end of the story. If we abandon the project, our credibility with the French and Norwegians will be undermined. The last is not a decisive consideration; but it needs to be borne in mind.

6. I am sending copies of this minute to the Chancellor of the Exchequer, the Secretaries of State for Energy, Scotland and Industry, Sir Robert Armstrong and Mr Robin Ibbs.

A handwritten signature in blue ink, appearing to be 'C' with a flourish underneath.

(CARRINGTON)



PRIME MINISTER

## GAS GATHERING PIPELINE

In Keith Joseph's absence abroad I am writing to let you have my views on David Howell's minute to you of 26 August. Unfortunately it will not be possible for a DOI Minister to attend your meeting on Tuesday.

There is in my view no doubt that it is in the interests of British industry that this project should go ahead. In the first place shortages of gas have proved a significant inhibition on the development of some energy intensive industries and this constraint could well emerge again once the current recession is past. The priority accorded to supplying domestic gas consumers means that any shortage of gas supplies is focused to a disproportionate extent on industrial users.

Secondly, the proposed gas gathering pipeline would provide a secure supply of ethane and other natural gas liquids which could serve as a petrochemical feedstock or could meet other industrial uses. To the extent that ethane is in some respects a superior feedstock than naphtha, petrochemical companies in Britain could secure an advantage over their Continental competitors. The poor prospects for petrochemicals in coming years and substantial surplus of capacity throughout Europe means that, even with these new materials, significant expansion can by no means be guaranteed. But without them serious contraction of UK petrochemicals seems virtually certain. I understand, for example, that BP Chemicals are seriously considering closing much of their petrochemical complex at Grangemouth if they cannot secure ethane from the gas gathering line.

Third, building the line could provide very substantial new work for supplier industries, notably the steel industry in supplying pipe, and the process plant industry. This does not by any means represent a crucial argument in itself for going ahead with the project. However it does, to my mind, underline the desirability of pressing ahead at the present time when these supply industries are desperately short of orders.

*Prime Minister  
Do I want to see the  
pipeline go ahead.*

*MM 28/1/11*

*ms*





I am copying this minute to the Chancellor, the Secretaries of State for Foreign and Commonwealth Affairs, Scotland and Energy, Sir Robert Armstrong and Mr Ibbs.

KB

KENNETH BAKER

28 August 1981

PRIME MINISTER

Attendance at the meeting will be:

Chief Secretary  
Hamish Gray + 1 official  
Alex Fletcher  
Robin Ibbs  
David Wolfson  
John Hoskyns  
Alan Walters  
Cabinet Office Secretary

The Foreign Secretary will not be present, but has put in a minute stressing the importance of going ahead with the pipeline. There may also be some comments from Industry (Mr. Baker) in writing on Tuesday, but they will not be sending a Minister.

Flag A - David Howell's minute plus  
Liverman Report

Flag B - Lord Carrington's minute

Flag C - CPRS paper of 31 July

Flag D - Note of Chancellor's meeting  
of 3 August

Flag E - Chancellor's letter of 13 July

28 August 1981



detailed negotiations were completed: this might take several months.

18. Some companies cannot gauge the extent of their potential interest in the project until further drilling has been carried out to define their reserves: this will take a year or two.

#### Summary

19. The companies have taken up a negotiating position and have formulated their demands accordingly. Some represent genuine concern and will have to be met if initial company equity investment is to be obtained.

20. Assurances will be necessary on gas prices, return on pipeline investment, preferential pipeline rights for investors, depletion controls, refusal to the use of competing lines, and on the availability of funds to complete the project. Clearer definition is required of the tariff regime and the rights and obligations of the parties. While some of the requests for assurances could be readily met, others are more difficult. Even if the conditions were largely satisfied, many companies might not be persuaded to invest. The process of getting enough companies to commit themselves is not likely to be completed within the timetable for commitment required by the project as now planned.

21. The companies' attitudes which I have reported are based on the concept of majority private sector investment at the outset, together with the associated risks. The approach of the companies would no doubt



become more positive, and their demands for assurances somewhat relaxed, if a different scheme were adopted - as many of them advocate - under which the Government or British Gas assumed more of the initial risk.

#### GENERAL ATTITUDE TO PIPELINE INVESTMENT

22. Several background factors influenced the companies' attitudes. They complained about the general fiscal regime in the North Sea and particularly about recent changes: there was now less confidence that future investment would go forward, particularly in the condensate fields which might not prove very profitable but which were essential for the viability of the pipeline. The current "oil glut" obliged them to impose the most stringent criteria for new investment. They were not naturally disposed to invest in common carrier pipelines on a public utility basis, even if relatively risk free. If it involved high risk to the investors, as the present project appeared to, oil companies would rather put their money into their main business of exploration and development than into pipelines.

23. Any interest shown by the oil companies in offshore pipeline investment appears only when it is a direct requirement for the development of a reservoir. Even then they do not want to invest any more money or to invest it any earlier than they need to for that immediate purpose. Hence the more positive approach of companies like Mobil for whom a new pipeline is essential for the transport of their gas as soon as possible, and the more negative approach of the majority who may not have gas available until the 1990's, or who think they can rely for several years on existing pipelines.

24. Most companies accept the need for a new pipeline system to bring ashore new supplies of gas and NGL's, but several (including Shell, Esso, Phillips, Elf, Total and Conoco) do not favour the integrated scheme. In part the views of these companies reflect the commercial assessment of their own interests, particularly for those who naturally wish to see their existing pipeline facilities used to the maximum. But companies also put forward the general argument that it is unnecessarily costly to invest, or to commit investment, prematurely.

25. Those who preferred other schemes and who had put them forward to the Organising Group were unconvinced by the Group's rejection. These companies were reluctant to say anything that might suggest they had abandoned their preference. Under pressure, they defined their attitude to investment in the integrated scheme on the assumption that this was the project favoured by the Government who would not give the necessary approvals for competing schemes. The attitude of this group of companies remained essentially negative. However, companies who argue for the use of existing facilities, such as Elf and Total in relation to the Alwyn field and the Frigg pipelines,



would be forced to re-assess their views if the Government made clear that this alternative was not open to them.

26. All companies stressed the high degree of uncertainty and risk, and most suggested that the only way to overcome this sufficiently to promote private sector investment was for the Government or British Gas to underwrite these risks initially by one means or other and to introduce private capital later.

27. It must be remembered that, for the companies, investment in the pipeline would be additional to the large capital commitments they would have to undertake to develop the fields from which the gas would come. This is an additional reason for hesitancy on their part.

#### SPECIFIC ASSURANCES AND CONDITIONS

##### Gas Prices

28. All companies insisted on the necessity for an assurance or understanding about the price which British Gas would pay for gas for the pipeline. The current practice of negotiating field by field - and sometimes separately with each licensee of a field - gave no assurance of gas development on a scale sufficient to justify the pipeline. Each negotiation was protracted, and many could not even begin for several years, since the field was unproved or inadequately delineated, and the reserves and production profiles uncertain. As a pre-requisite for pipeline investment, companies therefore demanded undertakings about the pricing regime that would apply. There seems no doubt that some form of undertaking or assurance on this score must indeed be provided if companies are to be persuaded to put up the initial equity investment on the basis proposed. Naturally the companies see this as an ideal opportunity to press their case for higher gas prices, and like OPEC and other gas producers to demand full thermal parity with oil prices. When pressed, the companies show some differences in what they would regard as a sufficient assurance, but it would certainly have to go beyond broad generalities and to guarantee a real impact on future price negotiations. Thus there would in turn be an impact - and possibly a very large one - on the private sector return and on the PSBR in future years. The considerations are set out more fully in Annex C.

##### Return on Capital Investment in the Pipeline

29. The companies are under the impression that investors could expect a real rate of return of about 5% on their pipeline equity. Like many of the factors, this cannot be looked at in isolation, since it is linked with the risk carried by investors, their obligations and rights - particularly any preferential rights to pipeline use (see para 30) - and with the tariff regime. However, companies were unanimous in regarding 5% real as too low to give any inducement to invest. A general view emerged that something of the



order of 10% real was required, though some companies were concerned about the impact on the tariffs to producers.

#### Preferential Rights for Investors

30. Unanimously, companies thought it illogical and unfair that investment in the pipeline, particularly early equity investment, should carry no additional rights for the companies as producers, and that the investors should remain on an equal footing with those companies who sat back until the scheme was launched. They agreed on the need to have some safeguards for late-comers, and most companies accepted that investors need not have absolute guarantees of available capacity. But they considered it would be equitable, and an inducement to invest, to devise an agreement combining a degree of preference for equity investors with some protection for other users. I think this should be possible.

#### Participation by Other Producers


31. While companies insisted that if they invested in the pipeline they should be granted advantages over those that did not, they were equally insistent that they would not invest at all unless a substantial number of others did likewise. It is difficult to quantify this, but my impression is that even the most positive - BP and Mobil - will not commit their funds unless other producers responsible in total for something more than half of the early supplies for the pipeline do the same. In any case, companies are unlikely to invest capital appreciably higher than the amount proportional to their share of the pipeline gas, so that unless the majority of the producers become investors the desired capital structure will not be achieved.

#### Tariffs

32. Companies appeared to accept the general lines of discussions so far in the Organising Group, particularly the concept of a ceiling in the early years. They were worried about the figures, and some suggested that a tariff of 8p per therm would be required for the adequate remuneration of capital, and that this would be the highest in the North Sea and unattractive to producers. But they could not assess the economic consequences for themselves except as part of the total picture including rate of return on investment, tariffs, and the price of gas. So no clear message emerged, except that the tariff regime would need to be more clearly defined before anyone invests.

#### Definition of Rights and Obligations

33. There was a general view that it was urgent to define the respective rights and obligations of investors, the pipeline operator, and producers. Some companies put this first or second in their requirements: without this, they said, we have no "prospectus" to put to our Board. It was a complicated business, on which much more work was needed. It would be simpler, some



suggested, and the management of the project would be more effective, if ownership and operation of the pipeline was entrusted solely to British Gas or to a small group which included them.

#### Fiscal Regime

34. Two points were made about taxation. First, the general tax regime for the North Sea was not conducive to the huge - and in some cases marginal - investment in the fields from which the pipeline gas would come. Companies hoped that confidence would be improved by forthcoming discussions promised by the Chancellor of the Exchequer. Second, the "guidelines" decreed that the project would not be a joint venture so that expenditure would not lie within the ring fence and would not be allowable against PRT or Corporation Tax. This inevitably made the investment much less attractive to the companies than other opportunities in the North Sea. Companies argued that this was a severe disincentive. To bring the pipeline expenditure within the ring fence would be a considerable inducement to investors. This of course is a statement of the obvious. Companies did not in general state it as a condition, but made it clear that they were concerned with the after-tax return so that in the absence of a concession on this point they would look for a higher gross return.

#### Depletion Assurances


35. All companies asked for assurances limiting the exercise of the Government's powers to delay or cut back production from those fields which might supply gas to the pipeline. They believed, rightly I think, that it would be feasible to devise assurances that the Government would be ready to give and that the companies would regard as an adequate safeguard. I enquired about their attitude if the Government limited such assurances to producers who were also investors in the pipeline, or gave better assurances to these companies than to others. Most companies thought this would be a reasonable and equitable inducement to investors, if made clear at the outset.

#### Assurances on Competing Lines

36. Some companies asked for firm assurances that the Government, if the integrated scheme went ahead, would not allow gas which had been assumed as a supply for that scheme to be transported through other lines or "competing schemes". They argued that to allow this would undermine the economics of the scheme and add to the risks of investors. It should be possible to satisfy the companies on this score, though care will be needed to protect the Secretary of State from criticism of misuse of discretionary powers.

#### Better Knowledge of Reserves

37. All companies outside the Organising Group claimed that better knowledge of the gas reserves was needed before they could commit themselves to investment. Some companies needed to know more about the size and nature of their own



reserves before they could judge how interested they were likely to be in the scheme. Gulf and Conoco, for example, would become more interested if further drilling were to confirm the more optimistic hopes for Block 15/30 - but this would not be known for a year or more, and in any case would not persuade them that they should invest in the pipeline. More generally most companies said they were not convinced that the reserves postulated by the Organising Group would in fact be found, and that without the Norwegian gas which had been hoped for earlier there would not be enough to make the project viable. Their requests for further information had been met by generalities and by refusal to disclose data which was confidential. This appears to be a genuine anxiety, and one which is naturally stronger with companies who are at one further remove from the information than the members of the Organising Group. The anxiety will not be totally removed by better access to data: there are speculative reserves included in the assessment and the robustness of the scheme to variations in the reserves depends on many other assumptions. However, the Department of Energy and the Organising Group might usefully consider what might be done to improve the confidence of the companies in the figures of reserves and production used by the Organising Group.

#### Separation of Onshore and Offshore Sectors for Financing Purposes

38. Most companies said they would be less disposed to invest in the onshore part of the integrated scheme than in the offshore part, since they were not concerned with the onward handling and marketing of the liquids. They argued that the investment required from the offshore producers would thereby be greatly reduced, and that capital should be forthcoming for the onshore facilities from companies with downstream interest in the liquids. Shell and Esso, who are discussing the possible use and expansion of Mossmorran with the Organising Group, are ready to make some of their onshore facilities available, but told me that they were not committed to providing any finance for their expansion: this would be a matter for negotiation with other parties. The finance required for the onshore development must depend on the outcome of the current discussions. The separation of financing arrangements as between offshore and onshore may lead to some complications but would appear to be a step that would give producers some positive encouragement to invest in the offshore sector. Most companies accept that under any such separation, facilities at St Fergus would count as "offshore" - important since early commitment is required for the St Fergus plant.

#### Doubts about the Integrated Scheme

39. A few doubts were expressed about the technical soundness of the scheme, but more concern about its economics and its ambitious scale. This led some companies to prefer a scheme that made more use of existing pipelines. Nearly all companies were worried, in the light of general experience in the North Sea, about cost overruns and the adequacy of the provision for cost escalation. Some suggested that this concern could be met by Government undertakings to guarantee that any increase in cost would be met, and by





completion guarantees. Most companies felt they needed satisfaction about the management of the project, but this concern took different forms; some would prefer to be directly associated with the management, while others would not but wanted to assure themselves of the competence and authority of the managing body, and argued against a widely shared responsibility that would lead to confusion and delay in decision-taking.

#### Amounts and Timing

40. Several companies were prepared to put figures to the proportion of equity capital they might subscribe if the conditions they had stated were met. These figures, which repeated those given to the Organising Group, generally represented the proportion of reserves attributable to the company. Thus BP mentioned 10%, Conoco 5%, Amoco 2.2%. As to timing, all companies foresaw a period of at least two months for the taking by their main Boards of a decision in principle to invest, from the time at which satisfactory assurances were given by the Government and a sufficiently precise scheme could be submitted for approval. Special factors could easily lengthen the timetable, e.g. constraints on annual budgets and their deadlines, or changes in company ownership (as currently with Conoco) or policy. The additional time needed for firm commitment would depend on the negotiation of agreements defining the rights and obligations of the various parties. It could be several months.

#### CONSIDERATION OF THE COMPANIES' DEMANDS

41. The oil companies are in a negotiating stance and have asked for a lot, including several things that could emerge only from more detailed discussion between the parties. They have also other objectives in mind besides the terms of investment in the gas gathering line: their hopes of changing the fiscal regime and the policy for gas pricing are examples. Moreover the companies see their negotiating position as a strong one, since they judge that the Government is anxious to press ahead and reluctant to abandon or modify the objective of majority private sector investment. On their side, with few exceptions the companies see no great urgency in building a new pipeline system, and many of them would be content to sit back and wait without undue risk to their prospects of field development, while others prefer alternative schemes. The benefit of the integrated scheme to an individual company is not easy for them to assess and unlikely to compare in its importance to the company with the importance of the total scheme to the nation: the boost the scheme would give to British investment and the added security of gas supplies do not figure in the companies' assessments. The Government's commitment to completion in 1985 is seen by the companies as unrealistic, and the desire for immediate decisions on financing as a further weakness in the Government's position. Thus the companies hope that the Government will go a long way towards meeting their demands.

42. Behind the companies' negotiating stance lies an area of genuine concern

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ANNEX A - TERMS OF REFERENCE

'On behalf of the Secretary of State, to hold discussions in August with each of the companies already identified as likely to have a major economic interest in the collection of gas from those areas of the UKCS which would be served by the integrated gas gathering pipeline. The purpose of these discussions would be to establish as closely as possible the terms and conditions on which these companies would be willing to give financial support to construction of the gas gathering pipeline through equity, loans or guarantees, and the level of that support which they would be prepared to offer. Without commitment on the part of HMG it should be made clear to the companies that their responses need not be constrained by the guidelines for the project which the government laid down last year. The appointed negotiator should then report to the Secretary of State by 24th August his conclusions on whether a financing scheme based initially on majority private sector support could be arranged including the terms and conditions, both directly and indirectly related to the project, which would be necessary to achieve that. Insofar as possible the negotiator should obtain commitments from the economically interested companies that they would be prepared to participate in such a scheme and maintain work on the project to the present schedule.'



about the viability of the pipeline investment. Some of the pre-conditions demanded by the companies are not unreasonable and will have to be met if there is to be any chance of persuading the companies to put up the initial equity investment. Among these are the assurances requested on preferential rights for investors in pipeline capacity, and Government undertakings on depletion powers and the withholding of consent for the use of competing lines: these should be feasible in principle, though no doubt care will be needed in their formulation. Much more difficulty attaches to any assurance on gas prices, though it is one of the essential pre-conditions: here vast sums of money could be at stake and the devising of a suitable assurance would be of critical importance (see Annex C). The requests for completion guarantees or other forms of underwriting cannot be met without changing the nature of the scheme and the balance of risk. The insistence of even the most positive companies that a number of others should also agree to participate in the equity could prove a formidable obstacle to getting any movement started in view of the widespread lack of enthusiasm. Even if all or most of the requests and conditions were met, some companies seem likely to require considerable inducements before they will contemplate pipeline investment.

43. The timing is critical. The assurances required, if the Government agrees to give them, will need careful working out. When proposals are put to the companies, unless it is to be on a take-it or leave-it basis, the companies can be expected to negotiate for something more so long as they see themselves in a strong position. Even when common ground is established, the companies have their domestic decision-taking processes to complete, and after the principles are settled there will be much detail to be worked out before investment is firmly committed. This will happen quickly only if all parties share a determination to meet deadlines and to devote the necessary resources to the task. But given all that, several months must inevitably elapse before equity investment by the companies can be assured.

44. Once the present log-jam is broken, there is always the possibility of a "band-waggon" effect as companies standing on the sidelines jump aboard to share in the benefits which their more adventurous competitors may enjoy. Moreover, those companies who need early pipelines but prefer alternative schemes could change their tune if the Government (with confidence that the integrated scheme was going ahead) firmly rejected those alternatives. But the response of the companies indicates that there is not likely to be any early break in the log-jam on the basis of initial majority private sector equity.

J G Liverman

24 August 1981

CONFIDENTIALSUMMARY OF RESPONSES FROM COMPANIES

(note : Records of each discussion are held  
by Gas Division)

Amerada (not an operator)

Hesitant because of constant changes in fiscal regime.  
Prefer to sell gas at platform and British Gas to take  
entire responsibility for pipeline.

Require assurances on gas prices, return on investment  
in pipeline (10% to 15% real), depletion powers.

If they invest, would confine to offshore sector  
and would contribute 4% to 5% of capital required.

General attitude : hesitant

Amoco

Interested in pipeline only if Lomond field goes  
ahead : That depends on gas price and further  
delineation.

Require assurances on gas prices, linked with thermal  
parity.

Doubtful about availability of reserves and economics  
of integrated scheme,

Require assurances on cost over runs, return on invest-  
ment, preferential rights in pipeline, depletion.

If they invest, would confine to offshore sector and would  
be prepared to contribute 2.2%

General attitude : hesitant

BP (Member of Organising Group)

Require assurances on gas prices linked to thermal  
parity.

other

Require equity participation by companies including  
particularly Phillips and Hamilton groups.

Propose return on pipeline of 10% real, preferential  
rights for early investors.

Regards tax regime for pipeline as severe disincentive.



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Require assurances on depletion.

Recommend separate financing of onshore and offshore.

If investing, would contribute 10%.

General attitude : positive

Conoco

Regard integrated scheme as too ambitious. Prefer more limited scheme using existing lines.

Proposals too vague about rights and obligations of the various parties : no clear "prospectus".

Degree of interest depends on field 15/30 ; development uncertain until tax regime "sorted out" and field delineated.

Require 10% real return on pipeline and preferential treatment on access and tariffs.

Require assurance on gas prices but accept some flexibility.

If investing, could contribute 5%.

General attitude : very hesitant

Elf

Opposed to integrated scheme. Prefer scheme using Frigg lines.

Doubtful about reserves and production profiles.

Require assurances about gas prices, apportionment of risk between investors and users, depletion policy.

Financial resources very stretched - no money to spare.

General attitude : negative

Esso

Prefer own pipeline scheme using FLAGS system. Regard integrated scheme as too ambitious. Do not think they have gas reserves "in foreseeable future" which could use pipeline.



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In discussion about use and expansion of Mossmorran for onshore processing.

General attitude : negative

Gulf

Unsure of company's reserves in pipeline area; will not know much more for a year or two; may not have surplus gas for many years. General lack of sufficient information. Require assurances on gas pricing, tariffs, management.

Prefer offshore/onshore investment split.

General attitude : negative

Hamilton

Require assurances on gas prices, depletion, maximum tariff.

Prefer commitment in stages.

Investment could be 2% to 3% of total, but conditional on participation by other companies.

General attitude : positive

Marathon

No surplus gas from Brae until mid-1990's. Early investment unnecessary and uneconomic from Marathon's point of view.

Require assurance on gas prices, depletion policy. Not enough information about reserves for pipeline. Investors should have preferential rewards and conditions.

Prefer onshore / offshore investment split. If assurances met, would invest 5%.

General attitude : hesitant

Mobil (Member of Organising Group)

Require assurances that competing schemes would not be approved.

Assurance needed on gas prices for condensate fields, and on depletion powers.

Require preferential rights in pipeline for early investors.



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4

Prefer different financing scheme, with strong "Interim position" in Government.

General attitude: positive

Phillips

Prefer different scheme.

Concerned about tariffs.

Reserves too speculative.

Require assurance on gas prices, escalation in cost of pipeline.

If invest, expect higher rate of return, might contribute 1.5%.

General attitude: very hesitant

Shell

Not in favour of integrated scheme.

Prefer maximum use of existing pipelines.

Do not expect reserves (except Fulmar) available to line.

Discussing use and expansion of Mossmorran for onshore processing.

General attitude: negative

Texaco (did not accept invitation to discuss)

Letter to Organising Group said company's reserves near pipeline too uncertain to warrant any sponsorship of this scheme.

General attitude: negative

Texas Eastern (not operator)

Consider scheme too ambitious.

Require completion guarantee and more involvement by Government.

Require 10% real on pipeline investment and preferential rights for investors.



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5

Require guidelines on gas prices.

Require assurances on depletion powers.

Doubtful about future gas demand in UK.

Prefer onshore/offshore investment split.

General attitude: hesitant

Total

Prefer other scheme using Frigg lines.

Require assurance on financial loss including effect of less favourable tax regime if Government insists on own scheme.

Require information on reserves, allocation of risks between investors and users.

Require preferential rights in pipeline for investors.

General attitude: negative





## ANNEX C GAS PRICES

1. The companies require some assurance about gas prices in order to provide confidence that future fields will be developed to an extent and within a time-table that will ensure the viability of the pipeline project. They have little indication of the price which British Gas would be prepared to pay, particularly for the gas from condensate fields. The recently concluded contract with Mobil, at a reported price of 16p per therm, is some indicator for associated gas, but the companies claim that even with escalation it would be too low to justify the development of the condensate fields on which the pipeline economics will heavily rely.
2. All the companies have suggested that gas prices should be fixed on a basis of thermal parity with crude oil or refined products and escalated by an oil or energy related index. This has been argued by the oil industry world-wide and there has been movement towards it in OPEC and elsewhere. It represents a negotiating position of the oil companies which goes beyond the immediate issues of the pipeline, so that more is at stake both for the industry and the Government. When pressed, the companies show some divergence in their approach, although all regard some assurance on prices as a pre-requisite for investment in the pipeline. The more extreme argument is that all offshore gas should be priced on a parity with oil, even associated gas (except insofar as the conditions of supply - namely the limited flexibility in varying the rate of production - justified a discount). The more moderate is that the cost of production from the condensate fields, particularly the smaller ones, will require gas prices of upwards of 25p per therm to make their development economic, and this points to a thermal parity formula; associated gas does not necessarily require a price of this order to justify field development.
3. Some at least of the companies would be satisfied with a more flexible formula which took account of the different types of fields. Some have suggested that a "floor price" could be defined, above which negotiation could take place based on the circumstances of individual fields. The concept of thermal parity linkage is capable of varying interpretations: some companies indicate that they do not necessarily mean a 100% relationship (except in the escalation formula). But clearly any formula acceptable to the companies must include some firm elements and figures: they will not be satisfied with generalities. Any statement which gives companies the concrete assurance they require must have the effect of reducing the negotiating freedom of British Gas. It might therefore result in their paying more for their supplies - and possibly substantially more - than if no assurance had been given. Any assurance directed at supplies for the pipeline would have to cover fields that may not be developed



until the late 1980's and beyond, so that gas prices would be influenced to the end of the century and later. Thus very large sums of money are at issue over long periods, and an assurance which raises gas prices beyond the level which might otherwise be negotiated would have a substantial long-term impact on the PSBR (although the impact could be moderated by taxation.) There are also international implications for the prices that might have to be paid in OPEC or other overseas gas.

4. Both British Gas and the oil companies appear to be giving some thought to a suitable assurance on prices. The problems on both sides are formidable, the Government must clearly be involved, and a solution will take time.

To be replaced  
Energy

PRIME MINISTER

In his minute below, Mr. Howell reports on John Liverman's discussions about the gas gathering pipeline. Liverman's conclusion is that it will not now be possible to arrange initial majority private sector financing in time to launch the project on that basis. Mr. Howell argues firmly that the Government should now authorise British Gas to underwrite the initial financing. He expresses his confidence that oil companies will begin to join in once the exercise is under way.

We can expect to hear a more sceptical view from the Treasury, and I am sure that your meeting scheduled for Tuesday will now be necessary.

At present we expect it to be attended by the Chancellor, Alex Fletcher, Hamish Gray, accompanied by a senior official, Robert Armstrong and Robin Ibbs. I think we should also add a Foreign Office Minister in view of the Norwegian interest. Do you agree? Would you want John Hoskyns, David Wolfson and/or Alan Walters, to join in?

MAR

26 August 1981

*A signed  
letter*



Prime Minister

GAS GATHERING PIPELINE

In my minute of 4 August I recorded my agreement with the Chancellor that we should make one final attempt, using an honest broker, to enlist financial support from the oil companies for the launching of the gas gathering project. The Chancellor and I agreed that Mr John Liverman should take on that role. He has now completed an intensive round of discussions with the companies. I attach a copy of his report.

Mr Liverman's report confirms that it will now not be possible to arrange initial majority private sector financing in time to launch the project on that basis. The Organising Group had reached the same conclusion. In Mr Liverman's round of discussion it was made clear that the companies were free to suggest changes in our guidelines or any other conditions they would need. Even then only three companies (BP, Mobil and Hamilton) - not nearly enough to take a majority share - showed a really positive response. Those that did show interest laid down major conditions which could not be met quickly, if at all. Recent changes in North Sea taxation have clearly soured company attitudes.

The idea of private sector financing at the outset is therefore now closed. If the project is to survive, major contract commitments will have to be made in the course of September. We therefore need to take a final decision on financing in the next few days. Your office has arranged a meeting on 1 September to discuss this in the light of Mr Liverman's report. Two courses are open to us:

- (a) to allow British Gas to provide the initial financial support necessary to launch the project;

(b) to reject that option on PSBR grounds and announce that the project has collapsed.

I am quite clear that we should now authorise British Gas to underwrite the initial financing. I am confident that once the project is launched on that basis and seen to be going ahead oil companies will start to join in. As Mr Liverman says, many of the companies are in a negotiating stance which will persist until they know that our minds are made up. Those who favour alternative piecemeal schemes will be forced to change their ideas. We should then be able to negotiate many of them on board by meeting some of the concerns Mr Liverman has identified. The PSBR burden and the call on public expenditure would be temporary.

The alternative of abandoning the scheme would, I am convinced, be both economically wrong and politically disastrous. Both the study carried out jointly by my officials and the Treasury and the CPRS report, recognised that the integrated pipeline was economically the most favourable solution for the nation. We have publicly expressed our support for the project on many occasions; its abandonment now would be a severe blow to the Government. Criticism of the delay in launching this project is mounting in Scotland, in the media and in Parliament. The critics include some of our own supporters. There is also anxiety in industry lest the major benefits of the project for suppliers, contractors, employment and the petrochemical industry be lost.

To abort the project on the grounds that it would add potentially to the PSBR would be inexplicable. We would be accused of abandoning a project of great national advantage, with a large net benefit to the economy on the grounds of economic argument which is, at best, debatable. It is not clear what our defence would be. The concept of "crowding out" other investment is really not an argument in this case. Whether the public or the private sector finances it initially,



there is surely an overwhelming case for a project which, for an investment of about £1.5 billion, will land some £25 billion worth of gas and which can be readily adapted in due course to the private sector utility pattern which we seek. Moreover the scheme is the best way of ensuring satisfactory gas recovery in the North Sea in the longer term. It is much the best way of minimising wasteful flaring. Perhaps even more important, this scheme would place us in an excellent position to bid for major new Norwegian gas discoveries which might otherwise go the European mainland.

I very much regret that because of my commitment to visit Japan I shall not myself be able to attend the 1 September meeting. Hamish Gray, who has of course been closely involved in this project, will represent me. I am copying this minute and Mr Liverman's report to the Chancellor, the Secretaries of State for Foreign Affairs, Scotland and Industry, Sir Robert Armstrong and Mr Robin Ibbs.

*David Chadwick*

pp Secretary of State for Energy  
26 August 1981

(Approved by the Secretary of State and signed in his absence)



GAS GATHERING PIPELINE  
PROSPECT OF MAJORITY EQUITY FINANCE  
FROM OIL COMPANIES

REPORT BY J G LIVERMAN

Conclusions	Paras 1 to 21
General Attitude to Pipeline Investment	Paras 22 to 27
Specific Assurances and Conditions	Paras 28 to 40
Consideration of the Companies' Demands	Paras 41 to 44
Annex A	Terms of Reference
Annex B	Summary of Responses from Companies
Annex C	Gas Prices.



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REPORT BY J G LIVERMAN

CONCLUSIONS

1. The general attitude of companies towards investment in the pipeline is conditioned by their stringent criteria for new projects, dislike of investment of "public utility" type, and their disquiet about the offshore fiscal regime and its impact on development. In addition several companies do not favour the integrated scheme: they prefer a staged approach with more use of existing pipelines.
2. This negative attitude is relaxed only when the companies see a direct link with proposed or prospective field development and can calculate a net advantage.
3. A positive attitude is shown only by those with an early need for pipeline connection and no alternatives readily available. Other companies will require inducements to invest and all require assurances.
4. The most important single assurance required is one about gas prices. This may be capable of solution, but it will be difficult. If it is to be resolved, priority must be given to the task. Even so, it will take time.
5. An assurance on gas prices alone will not be sufficient, though without it there is no prospect of initial equity investment by the companies, (apart from those - at present only Mobil - who have an agreed sales contract).





6. The companies will expect a higher rate of return - of the order of 10% real - on the pipeline than has so far been indicated.

*This is reasonable*  
7. They will insist on preferential rights of access to pipeline capacity for investors, though it should be possible to include safeguards for others.

8. Companies will put up equity capital only if a sufficient number of others do so, and some form of guarantee is given that the total of necessary funds will be available and the project completed.

9. Clearer definition of the tariff regime is required.

10. An essential condition for investment is that there should be a precise formulation of the rights and obligations of the various parties, and of the management arrangements for building and operating the pipeline.

← 11. Investment would be facilitated if it was allowable within the ring fence for tax purposes, but if not the companies would be looking for a higher rate of return in gross terms.

12. Companies outside the Organising Group complain of lack of information about the gas reserves assumed in the economic calculations. While some of these reserves are indeed speculative, the attitude of these companies might be favourably influenced if it were possible (within the limits of confidentiality) to make more information available to them.

13. Most companies would prefer the financing arrangements to be divided



between the offshore sector (including St Fergus) and the onshore, with different participants for each. It would be easier to get them to invest in the offshore sector, with its lower capital requirements, than in the whole project.

14. The companies will insist on government assurances that powers of depletion control will not be exercised so as to delay or reduce the gas available to the pipeline. Such assurances could be given without great difficulty. As an inducement, they could be limited to investors, or could be stronger for investors than for others.

15. They will insist also on a firm indication from the Government that gas will not be allowed to flow through alternative competing systems if the integrated project can take them. Early commitment of Alwyn gas, vital for the first years of operation, is specifically requested. It should be possible to do something on these lines.

16. The amounts that companies might be prepared to invest if their conditions were satisfied is roughly in proportion to their estimated reserves that would flow through the pipeline. For those companies that have shown a more positive approach (BP, Mobil, and the Hamilton Group) this totals rather over 15% of the equity. But even for these companies, major conditions have to be satisfied.

17. From the time that companies receive assurances that they regard as satisfactory, they will require two months to obtain approval in principle for the investment. Commitments of funds would not be made until more

MS1

PRIME MINISTER

In his minute below, Mr. Howell reports on John Liverman's discussions about the gas gathering pipeline. Liverman's conclusion is that it will not now be possible to arrange initial majority private sector financing in time to launch the project on that basis. Mr. Howell argues firmly that the Government should now authorise British Gas to underwrite the initial financing. He expresses his confidence that oil companies will begin to join in once the exercise is under way.

We can expect to hear a more sceptical view from the Treasury, and I am sure that your meeting scheduled for Tuesday will now be necessary.

At present we expect it to be attended by the Chancellor, Alex Fletcher, Hamish Gray, accompanied by a senior official, Robert Armstrong and Robin Ibbs. I think we should also add a Foreign Office Minister in view of the Norwegian interest. Do you agree? Would you want John Hoskyns, David Wolfson and/or Alan Walters, to join in?

Yes please  
MAQ

if available

26 August 1981

COVERING CONFIDENTIAL



**10 DOWNING STREET**

NOTE FOR THE FILE

WR  
has seen  
filed during  
last week

Please bring up to Willie Rickett during the last week of August. He must contact the Department of Energy and ask them whether the meeting on Tuesday 1 September at 1100 a.m. to discuss Gas Gathering Pipeline is to take place.

*ES.*

5 August 1981



MBPM -  
PM has already  
seen minutes  
of the mtg.

~~Mr. A. Duguid~~  
A. Walters.

PRIME MINISTER

DL

9/8

GAS GATHERING PIPELINE

I thought it would be helpful if the Chancellor and I met yesterday to discuss the report of Robin Ibbs submitted on 31 July to see if we could agree on the next steps without the need to trouble you at this stage. Hamish Gray and Alex Fletcher joined in our discussion.

We agreed that one further and last attempt should be made to enlist financial support from the oil companies. I must confess that I am not optimistic that this attempt will be successful but I accept we need to establish as precisely as we can the terms, including if necessary modification of the guidelines, on which a significant number of companies would be willing to participate at this stage. We should then be in a better position to assess the options open to us.

Robin Ibbs suggested in his report that in such an approach to the companies we should tell them that, if the pipeline failed to be launched as a private sector venture, it would be abandoned for the foreseeable future. I do not believe that this would have the desired effect on the companies and indeed would be politically wholly unacceptable. The Chancellor and I therefore agreed that this last attempt should be entirely without prejudice to our final decision on the project.

The Organising Group would not be the appropriate body to conduct these further discussions, given the unsuccessful efforts they have already made. We see merit in Robin Ibbs' suggestion of an independent "honest broker" and I will agree a suitable name with the Chancellor. Our broker will need to make it clear to the companies that this is indeed our last attempt and that, entirely



without commitment on HMG's part, it would be open to the companies to suggest any changes to our original guidelines, or conditions on gas prices, which would be essentially pre-conditions for their financial support.

Time is now very pressing since major expenditure commitments will have to be made in September if the project is to be kept on schedule. It is essential that we take a final decision in the first few days of September and your office has arranged a meeting for 1 September.

I will report the outcome of our initiative in time for this meeting, together with an account of the options open to us. One of these will be the Morgan Grenfell scheme. I have therefore asked the Chancellor to arrange for his officials to study its implications in detail.

I am copying this minute to the Chancellor, the Secretary of State for Scotland, Sir Robert Armstrong and Robin Ibbs.

A handwritten signature in dark ink, appearing to read "David Hunt", with a stylized flourish at the end.

pp Secretary of State for Energy  
4 August 1981

(approved by the Secretary of State  
and signed in his absence)

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~~to Sir R. Armstrong~~  
Mr. Hobs  
Mr. Holtzman  
Mr. Duguid



Dominic Austin 2  
Mr. Hovels and the  
Chancellor have agreed  
to call in a "third  
party" to negotiate with

NOTE OF A MEETING HELD AT 11 DOWNING STREET ON MONDAY, 3 AUGUST, 1981

Present:

Chancellor of the Exchequer  
Mr. Middleton  
Mr. Christie

Secretary of State for Energy  
Minister of State for Energy  
Mr. T.P. Jones

Minister for Industry and Education, Scottish Office  
Miss Ross - Scottish Office

the oil companies.  
You may need to  
take a meeting in  
early September; we  
have arranged a  
provisional date for  
it.

GAS GATHERING PIPELINE

The Secretary of State for Energy said that since the meeting with the Prime Minister had had to be cancelled, he had sought this meeting with the Chancellor in order to see whether a way forward could be found without further troubling the Prime Minister at present. The Chancellor's own suggestion in his letter of 13 July had been to make one last try over the next few weeks to secure majority private participation in an integrated pipeline. The suggestion had been to ask someone quite independent of the oil companies and BGC to contact all the interested parties and to conduct an assessment of the minimum conditions each would require for participation in the line. For his part, he still believed that the Morgan Grenfell scheme was the best, but he was now prepared to agree to the Chancellor's proposal, on two conditions:-

(i) that there should be no suggestion to the oil companies that the alternative to a scheme agreed with them was abandonment of the project; and

(ii) the result should not pre-judge the final decision on whether or not to go ahead with an integrated scheme. He hoped that on this basis it would be possible to

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reach final decisions in the first few days of September.

2. The Minister for Industry and Education, Scottish Office lent full support to this proposal, adding that there would be serious political consequences if there were to be any suggestion of abandoning the project.
3. In discussion some anxiety was expressed that if the Government entered into negotiations with the oil companies when it was known they remained committed to the project, this would put them in a tactically advantageous position. It was suggested that the right stance would be a neutral one - a firm commitment to continue with the project did not have to be given, and while the possibility of abandonment was implied this would have some leverage. The oil companies would appreciate that this was the Government's last shot at involving them, and it should be possible to get from them a frank statement of where they stood.
4. In discussion of who might be asked to carry out the negotiation on behalf of the Government, there was unanimous support for a candidate suggested by the Secretary of State for Energy, Mr. John Liverman, a retired Deputy Secretary at the Department of Energy.
5. The Chancellor, summing up the discussion, said that there was agreement that negotiations should be conducted over the next four weeks with the oil companies and other interested parties to obtain a clear picture of the conditions under which they would be prepared to go ahead with an integrated pipeline project. In these circumstances the meeting with the Prime Minister could be put off until very early in September, when final decisions would be taken. It had been agreed that Mr. John Liverman would be the best person to carry out the negotiations and he would now be approached by the Secretary of State for Energy. Mr. Howell would also then send a minute to the Prime Minister reporting what had been decided, and suggesting a further meeting to take final decisions on the question very early in September.





Circulation

Those present  
Financial Secretary  
Minister of State (C)  
Minister of State (L)  
Sir Douglas Wass  
Mr. Ryrie  
Sir Anthony Rawlinson  
Mr. Downey  
Mr. Burgner  
Mr. Christie  
Mr. Wicks  
Mr. Todd  
Mr. Ridley  
Mr. Cropper  
Mr. Cardona  
Mr. Johns - I/R  
Mr. Lankester - No.10  
PS/Secretary of State for  
Scotland

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Qa 05647

To: MR LANKESTER

From: J R IBBS

*Pmi Minutes*  
*The Chancellor and*  
*Mr Home will attend*  
*this meeting accompanied*  
*by officials.*

31 July 1981

Gas Gathering Pipeline

1. In your minute of 20 July the CPRS was asked to clarify the factors causing the apparent current impasse on the gas gathering pipeline. In the short time available the CPRS has discussed the issues involved with the Secretary of State for Energy and his officials, Treasury officials, Sir Denis Rooke as Chairman of the Organising Group and representatives of BGC, BP and Mobil as members of the Organising Group. We have also had brief discussions with officials in the Scottish Office and Department of Industry.

2. The number of issues involved in a project of the magnitude and complexity of the Gas Gathering Pipeline (GGP) are such that exhaustive coverage would run to many tens of pages. In what follows we have tried to restrict the analysis to the minimum necessary to answer two simple questions -

- (i) why is there an impasse?
- (ii) what options are available to break the log-jam and what are their respective advantages and disadvantages?

The situation is extremely complex and in this short note consideration has been concentrated on the central issues.

3. To understand why there is an impasse it is necessary first to explain a little of the background.

Background

4. The concept agreed at E Committee last summer was that an Organising Group should develop proposals for constructing an integrated gas gathering line as a private utility transmission company. The project would be in the private sector, BGC would have 30 per cent of the equity but this would have only a small effect on the PSBR because equity was not seen as a major source of finance.

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5. The Organising Group (BP, Mobil and BGC under the Chairmanship of Sir Denis Rooke) was given confidential guidelines embodying features of E Committee's decisions. Key points in the guidelines are:

(i) that the pipeline should be built by a company not a joint venture (a main point here was to prevent North Sea producers setting off investment in the pipeline against tax liabilities arising from field incomes);

(ii) that the tariff charged for use of the pipeline should be calculated on a cost of service basis (so that the natural monopoly position of the pipeline would not be abused to yield excessive profits and deter new field developments);

(iii) that investment in the pipeline should not carry with it rights to use the pipeline (to prevent investors either pre-empting spare pipeline capacity or sub-leasing at exorbitant rates when other producers might wish to make use of it).

6. The Organising Group has pushed ahead with the technical work on the project, and this has gone well; detailed design is nearly complete, the project is on schedule for completion in 1985 and to keep to that deadline major contracts involving commitments of hundreds of millions of pounds must be placed this year starting in September. However, the Organising Group will not undertake these commitments without financial backing and, in spite of extensive discussions, its efforts to develop proposals on financing have come to nothing. (A recent attempt by the Bank of Scotland to raise £700m. of interim finance failed because a guarantee of completion was needed which the potential participants in the scheme were not willing to provide.) To understand why the oil companies, who provide the key to the financing, are unwilling to participate on current terms, it is necessary to appreciate the economics of the gas gathering line.

Economics

7. In national terms there is an overwhelming case for development of the gas in the northern basin of the North Sea; the discounted value of the reserves (possibly a conservative one at that) is some £25 billion

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against pipeline costs of £1½ billion (1981 money). This calculation is, of course, in terms of total costs and benefits not in terms of profit and loss as a private company would see it; because of the distorting effects of high taxation in the North Sea the outstanding return in national terms does not necessarily imply that private capital will be available to finance a project.

Integrated Pipeline compared with Multiple Developments

*whether the gas will be developed*

8. However, the key question is not so much whether the gas will be developed but what is the most economic way of doing so. The alternative to the integrated gas gathering line is to allow multiple developments of the gas fields through the two existing gas pipelines (FLAGS and Frigg) with as many new separate pipelines as may be necessary. In other words follow the same development procedure for gas as has happened on oil. The integrated Gas Gathering Pipeline costs more than its multiple alternative (for both onshore and offshore construction £1.5 billion against a broad brush estimate of £1.2 billion for the best multiple scheme that Department of Energy officials have devised). Nonetheless it has numerous advantages which led to its endorsement at E Committee, amongst these are:

- (i) it shows a higher economic return in national terms than the multiple scheme and is robust to variations in the main assumptions (nevertheless the multiple scheme still offers a very good return);
- (ii) it has been carefully sited and sized with an eye to future exploration and development and should be able to service whatever the reserves may ultimately turn out to be;
- (iii) it will provide competition for the existing gas pipelines (FLAGS and Frigg) thus reducing the amount of money from gas development going to the existing pipeline owners who could otherwise exploit their monopoly positions;
- (iv) it guarantees early collection of all gas liquids and their bulking for potential petrochemical use;
- (v) it offers a better opportunity of attracting gas from the Norwegian sector;

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(vi) it offers UK companies the best chance of receiving the bulk of the development contracts.

Disadvantages of Integrated Pipeline

9. However, it also has some disadvantages against the multiple alternative:

(i) it is a major project and therefore arguably more liable to cost over-runs than individual developments;

(ii) more important, it entails a greater risk than multiple developments because it effectively involves committing capital ahead of time and investing for the future. The whole length of the integrated line must be built to take advantage of the 'associated' gas shortly available from oil fields. However, the economics of the line depend only to a minor extent on associated gas, the principal return will come from development of unassociated gas fields along the route of the line. In the alternative of having multiple pipelines these are built only when gas fields are to be developed; in the integrated approach the pipeline is built first in anticipation of individual field developments.

Why the Impasse?

10. It is the above two disadvantages that have been at the heart of the oil companies reluctance to participate. It is a risky project and the cost of service approach means that if the risk pays off the benefits accrue not to the shareholders but to users of the pipeline in the form of lower tariffs. Oil companies do not traditionally invest in projects with utility returns and the present guidelines give them no incentive to participate. It is a perfectly rational policy for any potential user of the pipeline to stand back and let another party use up financial resources and stand the risk.

11. The particular risk that the oil companies are most concerned about is that not enough gas will be forthcoming in the early years of the pipeline to provide a satisfactory return (the early years are the most important in calculating financial returns). Moreover, this could

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initiate a vicious circle; if the gas were not forthcoming, the cost of service approach would mean higher tariffs which in turn would inhibit gas development. The oil companies point to the fact that the rate of production of gas is not subject to pure market forces and involves risks that they cannot reasonably assess. First of all the Secretary of State for Energy can determine the rate of development through his powers of approval for individual fields (the Department of Energy say this problem can be overcome and they can provide a guarantee to the oil companies that they will not intervene in gas production through exercising depletion controls); more important, BGC through its current monopsony powers sets gas prices and through these determines the rate of development, thereby operating an implicit depletion policy. (At present BGC are blocking exploitation of relatively low cost gas in the Southern Basin by not bidding.) It is the price of gas that is the major stumbling block to progress on the project; it not only determines an oil company's direct return on the gas it develops but the price offered to other producers will determine the volume put through the pipeline and therefore the financial return.

The Way Ahead

12. It is common ground that the project cannot move ahead in its current form and on the current terms. In essence there are four options:

- (i) abandoning the GGP and adopting the multiple approach;
- (ii) constructing an integrated line at a later date;
- (iii) going far enough towards meeting the oil companies' demands for participation to convince a sufficient number of interested parties before the end of September that the project is viable enough for them to undertake the immediate commitments;
- (iv) going ahead with the integrated pipeline, at least initially, in the public sector.

The Multiple Approach

13. The advantages of the integrated line over the multiple approach were described previously (paragraph 8). In short the integrated pipe-

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line seems to serve the national interest better but the multiple scheme involves a later commitment of capital and therefore offers more flexibility to meet changing circumstances.

Constructing an Integrated Line at a later date

14. It is arguable that delay in constructing the integrated pipeline would lead in practice to the multiple approach. This is the third time that the prospects for an integrated gas gathering pipeline have been evaluated and failure again to launch a scheme would only serve to increase scepticism that the project would ever succeed because of its inherent complexities and the different interests involved; at the very least it would be more difficult next time around to persuade companies to dedicate people and resources to an examination.

15. In addition, delay carries with it further disadvantages:

- the likelihood is that gas would be lost to the prospective line, UK Statfjord, North Alwyn and possibly Beryl;
- the prospects for petrochemical use of NGLs brought ashore by the line would recede;
- UK companies hoping for major orders would be disappointed;
- once the prospect of an integrated line receded the Norwegian pipeline would become an attractive outlet for UK gas producers.

Meeting some of the Oil Companies' Demands

16. There seems little doubt that part of the oil companies' present reluctance to participate in the financing is a negotiating ploy; they know that their support is needed and that the Government is keen to see the line go ahead quickly, while they themselves can in many cases afford to delay, negotiating for the best possible deal on gas price, taxation and a system adopted to suit best their own individual interests. Their shopping list is long, including

- gas pricing as the primary concern
- the tariffs to be charged on the pipeline
- the financial return on the pipeline

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- access to capacity in the pipeline
- tax offsets
- depletion policy
- scope of the project.

17. It has emerged from our enquiries that an improved gas price would not itself ensure that oil companies would participate in the pipeline; they would need some direct incentive to invest in a line that offers only a utility type return. One possibility would be to offer investors in the pipeline first refusal on capacity. What other concessions might be necessary could only be found through detailed negotiation.

18. However, the critical factor without which there can be no progress is price. Behind the wide gap in what BGC is currently willing to offer for gas (around 16p/therm) and what the oil companies are currently demanding (26-29p/therm) lies a qualitative difference in pricing mechanisms. The oil companies want a posted price for gas in the same way as there is a common price for North Sea oil thus allowing a wide variety of returns; BGC currently price gas on a cost plus basis in effect giving the companies a fixed return and capturing as much as possible of the available economic rent (gas production costs for fields supplying the pipeline can vary from 2p/therm for associated gas to 30p/therm for a small dry gas field). Although BGC are currently urgently reviewing their pricing policy, our interview with Sir Denis Rooke did not give any grounds for optimism that a compromise satisfactory to the oil companies would be possible without Government intervention. It is possible that a compromise might be achievable on the basis of a different posted price for each of the different categories of



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gas - associated, dry, condensate - with a distinction between that already discovered and that to be explored for.

19. In addition, and as an aid to successful completion of these negotiations, two possibilities exist for making the integrated scheme more attractive to the oil companies:

(i) initially utilising existing onshore facilities at Mossmorran thus reducing the overall cost of the scheme;

(ii) there may be advantage in splitting the project into two, onshore and offshore, to encourage the chemical companies, who would benefit from the onshore facilities, to participate thereby increasing the number of economically interested parties that might invest.

20. However, the key constraint to this approach is time. Could negotiations be completed in time for letting contracts in September? A possible mechanism for the negotiations would be for discussion to take place with a small representative group of the producers; if, after negotiation, they believed the basis for a viable project had been established, it would be up to them in turn to convince the other producers. Needless to say the negotiations would require a very skilled Government intermediary capable of puncturing negotiating stances.

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21. The recent signing of a contract between BGC and Mobil for Beryl Gas at 16p/therm has been put forward as likely to encourage other companies to complete negotiations. However, this is rather a special case involving associated gas and it is whether prices will be sufficient for the higher cost unassociated gas field development that is the primary concern of the oil companies.

Going Ahead in the Public Sector

22. The Department of Energy argue that such negotiations would make no progress and that a necessary pre-requisite to bringing negotiations with the oil companies to a successful conclusion is to announce in advance that the project is definitely going ahead in the public sector. The basis for this view is that, they believe, the companies do not think that the Government will put a project of this magnitude in the public sector. Therefore as time goes on the oil companies believe that the Government will become increasingly desperate to involve the private sector and that their negotiating hand grows stronger. Alternatively, if the project is abandoned the multiple scheme offers the companies advantages in terms of greater tax offset. In the view of the Department of Energy a prior announcement that the project would proceed in the public sector would break the current deadlock because the companies would not wish to see BGC in sole control of the pipeline. Thereafter there would of course be further negotiations in settling the terms on which private companies came in, with gas prices as one of the factors.

23. The key question is whether Ministers would be willing to see the whole of the capital cost of the Gas Gathering Line fall on the PSBR initially, even though it would come off the PSBR again when the pipeline was subsequently privatised. In comparison, the capital cost of the multiple alternative would be tax deductible and hence it would also increase the PSBR; but its timing would be later than that of

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the GGP and the total effect smaller. The table below illustrates the level of expenditure involved in the GGP and the multiple alternative.

	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1985</u>	<u>1986</u>
<u>GGP</u>						
Pipeline	60	230	470	450	180	NIL
<u>Multiple Alternative</u>						
Pipeline				300	350	NIL

- Note 1: the above table excludes the associated Field Expenditure which is tax deductible and would vary between the schemes.
- Note 2: the timing of pipeline expenditure on the multiple alternative is particularly uncertain and the figures shown for 1984 and 1985 could be brought forward into 1982 and 1983.
- Note 3: the multiple alternative assumes some gas fields are deferred, which would reduce the level of gas supplies. Whether other fields would be brought forward to maintain the same energy production profile is a separate depletion issue, which could involve extra PSBR costs.

Thus during the initial period, which will in any case be one of heavy pressure on the PSBR, the GGP would make greater claims on Exchequer finance unless it were successfully privatised at a very early stage in which case it would constitute only a very small temporary burden.

24. The Department of Energy view that the oil companies would not like to see BGC in control of the GGP is certainly true. However, the CPRS is not convinced that public financing of the line will in itself other <sup>investors</sup> necessarily cause to come in, if there are doubts about the basic economics of the line.

Removal of BGC's Monopsony

25. Overhanging all these issues is the question of the possible removal of BGC's monopsony. If BGC's monopsony was removed, it would in theory give the companies the necessary reassurance on price that they need. However, it is not as simple as this. The removal of BGC's monopsony powers would not in itself be enough to encourage the oil companies to participate. If BGC's monopsony were removed and exports not permitted, there is a good chance that the ensuing rapid

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development of the cheaper cost Southern Basin gas would serve to depress prices in the UK. This would discourage development of the higher cost Northern Basin fields feeding into GGP on which its economics depend. To ensure the economics of the GGP the oil companies would therefore require reassurance that depletion controls would limit production from the Southern Basin, if BGC's monopsony were removed.

26. We understand the Secretary of State for Energy intends publishing a White Paper on the possible removal of BGC's monopsony. It is difficult to foresee what the effect of this uncertainty would be on the GGP. On the one hand it is arguable that oil companies would be reluctant to agree any prices with BGC until they knew definitively about the monopsony and depletion policy; on the other hand BGC might not be interested in negotiating prices whilst the White Paper was under discussion since it would be unclear where prices would eventually settle. Sir Denis Rooke was adamant when we saw him that if BGC's monopsony were to be relaxed BGC would not accept the total financing risks of the pipeline. (This is in effect the same argument as the oil companies are using. BGC will accept all the risks if they have control over prices; the oil companies will not accept any of the risks unless they have some reassurance on prices).

27. Logically both depletion policy and the question of BGC's monopsony should precede decisions on the GGP. Depletion Policy, the prime decision, determines the rate at which UK gas resources are developed; the question of BGC's monopsony relates to the most economically efficient way of bringing the gas to the market; the GGP concerns the physical way in which gas is transported to the market and is therefore a secondary decision. If the GGP is to be held to the present timetable of operation in 1985, Ministers have to take a decision on it before the questions of monopsony and depletion policy are settled.

CONCLUSIONS

28. It seems to the CPRS that an integrated pipeline would best serve the national interest - it would ensure maximum recovery of gas, it provides the best basis for underpinning the UK chemical industry with low cost feedstock and, it would maximise the construction orders

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let to UK industry. However, if the GGP is not built, most of the gas in the Northern Basin will not be lost, it will be developed less efficiently through multiple pipeline developments.

29. It is clear that with the present guidelines and BGC's posture on price there is currently no scope for the project to progress as a private sector venture on a normal commercial footing. Moreover it is also clear that substantive negotiations involving movement by all parties that might enable it to go ahead are not taking place. Some initiative is necessary.

30. One possible way forward, the one favoured by the Department of Energy, would be to decide that because the GGP is in the national interest, the project should be launched initially in the public sector, with an intention of bringing in private sector participants later. However quite a lot of easement, especially on price, would be necessary to begin to make the project attractive to such participants; this would take time. We are not convinced that if the pipeline was going ahead in any event, participants would want subsequently to come in unless the return was very attractive.

31. If Ministers are not willing to take the risk that the GGP might remain on the PSBR for a considerable time then the CPRS would suggest that an alternative route is the converse approach. This would consist of telling the potential participants that, in the national interest, the Government was prepared to make one last effort to launch the pipeline as a private sector venture, but that, if this failed then the GGP would be abandoned for the foreseeable future. It would be made plain that the Government was willing to make concessions on the guidelines and, through BGC, on gas price in an effort to bring about the project; this easement would provide a positive incentive for movement from present negotiating positions. If nothing came of it, the potential concessions including those on price would be withdrawn. It would be made clear to the companies that failure to respond to this initiative would be frowned on. The Government would arrange for an independent "honest broker" (possibly a consultant with oil knowledge) to see, within a fixed period, whether a reasonable compromise would be struck between the potential private sector participants and BGC.



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It is not clear how much movement on gas prices and the guidelines would be needed to secure sufficient participation by the oil companies. The concessions required could be considerable.

32. I am sending a copy of this minute to the Chancellor of the Exchequer, the Secretary of State for Energy and to Sir Robert Armstrong.

*JR*

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PRIME MINISTER

*MF*

Gas Gathering Pipeline

You agreed that Robin Ibbes should conduct a quick review of the gas gathering pipeline proposals to see if a way can be found out of the current impasse. This work is already under way, and Robin will report back to you at the end of next week, with a view to your holding a meeting with Mr. Howell and the Chancellor on Monday, 3 August.

You also suggested that we might ask Ken Berrill for his advice on the possible financial arrangements for the project. I really think this would be unwise. If Robin got to hear of it, as he would be bound to if Ken were to start making enquiries, he would - I believe, take it very badly.

---

*A. Lloyd* Duty Clerk  
pp TPLANKETER.

21 July, 1981.

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R H



Blind cc: Mr Wolfson  
Mr Duguid  
Mr Walters

10 DOWNING STREET

From the Private Secretary

20 July, 1981

AF 31.7.81

Gas Gathering Pipeline

The Prime Minister has seen your Secretary of State's letter dated 14 July to the Chancellor in which he requests an urgent meeting to take decisions on the Gas Gathering Pipeline; she has also read the Chancellor's letter of 13 July.

The Prime Minister is disappointed that a project of such national importance has apparently reached such an impasse and is eager that a way through be found. Given the complexity of the current situation and the wide difference of views between your Secretary of State and the Chancellor, she has invited the CPRS, as a third party, to clarify the issues involved prior to any discussion. This will involve discussions with your Secretary of State, the Treasury and possibly also Sir Denis Rooke and the current Organising Committee. Given the overall urgency, the intention is to have the CPRS report ready as background for a discussion on Monday, 3 August. I trust your Department will give Mr Ibbs all the assistance he needs in preparing his report.

I am sending a copy of this letter to John Wiggins (HM Treasury), Gerry Spence (CPRS) and David Wright (Cabinet Office).

T. P. LANKESTER

Julian West, Esq  
Department of Energy

SP

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Yes - I should be  
grateful if Robin would  
do a visit  
in the Spring period. Would  
to be attended  
do ask the  
I will for  
I don't now  
I don't know  
I don't know  
I don't know

Prime Minister

This project is going to  
collapse unless we take urgent  
action to find a way out of  
the impasse. he must somehow  
ensure an adequate return to the  
oil companies, and this must  
mean BGC paying a decent price  
for the gas. I strongly support -  
in fact 17 July 1981  
my suggestion - the  
idea that Robin Ibb should find a  
way through - by talking to Energy,  
BGC and then, if necessary, the oil  
companies.

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Qa 05636

To: MR LANCASTER  
From: J R IBBS

Gas Gathering Pipeline

1. I have read the recent correspondence on the Gas Gathering Pipeline and this is apparently now at an impasse.
2. In his letter of 13 July to the Secretary of State for Energy, the Chancellor proposes that the impasse might be broken if BGC can be prevailed upon to give the prospective participants some reasonably firm assurance on the price which they would be willing to pay for the gas. He further suggests that someone quite independent of all the interested parties could produce an assessment of the minimum conditions.
3. In his response of 14 July the Secretary of State for Energy rejects the proposal and is of the view that it would get nowhere and lead only to further delay and loss of credibility. He suggests that the only way forward is for the integrated pipeline to be financed initially by the Government; he believes that only a prompt and firm commitment by the Government to go ahead regardless will bring in the private companies. Because of the urgency he wants a meeting to discuss the matter with the Prime Minister.
4. It is difficult to see from the correspondence how a meeting could easily lead to a decision on this matter since there is such a clear difference of opinion between the Chancellor and the Secretary of State for Energy on what may still be possible in terms of persuading oil companies to participate in a joint public/private project.
5. Because of our very heavy current workload in the CPRS, I cannot offer to do a major study of this problem. However, if the Prime Minister thought it would be helpful we could, if asked, do a quick review to clarify in somewhat greater detail just why the Secretary of State believes that a joint venture is out of the question. We might then be able to make an assessment of what would be necessary to bring this about and what the chances of success

Flag A

Flag B

Agree?

12

17/7

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might be. But it is impossible to guarantee that this would end up in a substantial advance on the impasse in the recent correspondence.

6. If we were to carry out such a review it would be essential that we had a clear remit from the Prime Minister which was accepted by the Secretary of State for Energy.

7. I am sending a copy of this minute to Sir Robert Armstrong.

[David Wilson - May 2 - has suggested that we let BGC carry out the project. But that is undesirable in itself, and the so-called Morgan-Gentle financing solution is a transparent device which the Chancellor is firmly against.]

R.  
17/5

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Cc J Vesekes

A Duguid

A Walker

B

SECRETARY OF STATE FOR ENERGY  
CHANCELLOR HOUSE SOUTH  
MILBANK LONDON SW1P 4QJ

01- 211 6402

The Rt Hon Sir Geoffrey Howe QC MP  
Chancellor of the Exchequer  
H M Treasury  
Parliament Street  
London SW1

14 July 1981

Dear Sir,

Thank you for your letter of 13 July on the gas gathering pipelines.

There are a number of comments in your letter which I simply cannot accept. It also fails to understand or take account of the oil companies' real motives.

Morgan Grenfell have suggested a way in which they consider the initial financing of the pipeline would not be a charge against the PSBR. Even if you do not accept their argument, the key point is that any PSBR addition would be, in my judgement, at most for two years and probably much less. The alternative under which fragmented pipelines were built by the companies and the expenditure then offset against CT and PRT would most certainly do permanent damage to the PSBR. The paper jointly agreed by our officials indicated that, if the integrated system were successfully privatised, the PSBR costs would be lower than these of the fragmented approach. We should not in my view be so hypnotised by PSBR theology as to treat a wealth-creating capital project as if it were an outlay yielding no return for the nation.

If the scheme is financed initially in the public sector, it may well be, as you say, cheaper to use the NLF although BGC claim that their own credit rating is such that they can obtain attractive rates.

You say that the E Committee proposal was a non-starter from the outset. I do not accept this. The indications at the time were that it would succeed. I am bound to say, however, that the reduction of BGC's role, largely at Treasury insistence, and hence the downgrading of HMG's commitment to the project certainly did not help in our subsequent negotiations. The imposition of additional North Sea taxes, about which I expressed concern at the time, has certainly also not helped the oil companies to take an interest in the pipeline. But I have no doubt that, when positive leadership is given by the Government, their involvement will be forthcoming.

You are wrong about Denis Rooke. Rooke may be a difficult man but there is no basis at all for questioning his integrity and commitment. From the start he was determined to make the gas gathering pipeline work and as overwhelmingly the major customer he was an obvious candidate as Chairman of the Organising Group. The objectives of paying lower gas prices than the high oil-related prices the producers want is not only a natural one for BGC, it is totally in the national interest. It is completely in line with the Prime Minister's strongly expressed wish that British industry should be protected as far as possible from sky-high gas price demands by the North Sea companies, both British and foreign.

I have considered, as the Prime Minister suggested, whether it might be possible to enlist the support of the private sector by relaxing the guidelines we laid down for the project. The two key points in the guidelines are the 'cost of service' approach and the choice of a company structure rather than a joint venture, for both of which there were good reasons. The cost of service approach means that tariffs could be limited to the level necessary to yield a fair rate of return on investment in the pipeline, thus avoiding any risk that the owners could exploit their monopoly position to make excessive profits at the expense of other producers. The decision against a joint venture approach was of course designed to avoid the pipeline being financed largely by tax relief, with the PSBR consequences I have mentioned above.

The real situation is that, whilst they would no doubt welcome a relaxation of the guidelines, the oil companies want more. Many of them hope that we will abandon our proposals and leave the way clear for their own piecemeal schemes which will serve their interests but not those of the nation as a whole. All the companies see our need for financing as a golden opportunity to force up gas prices.

Your proposal is that the oil companies should yet again be asked what their minimum demands are for coming in. In my view this suggestion is totally out of line with the commercial reality. Not only have the oil companies already been asked and replied with predictably unacceptable 'shopping lists' but it would be absurd to imagine that they will reduce their demands at this stage in the negotiations. Their terms will only change when they know that we are going ahead and that there is no alternative open to them, not before.

You refer to the multiple scheme, which E did not favour, as now being 'the safer option'. This contrasts markedly with the conclusions reached jointly by our officials that the integrated scheme is highly economic and preferable in national economic terms to even the most favourable pattern of piecemeal development which could result if we abandon our ideas.

/Further.....

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-3-

Further delay by asking oil companies yet again the same question - with the obvious and predictable answer - will in my view gain absolutely nothing. All it will do is to lose us still more credibility and further the demise of the integrated scheme. The only thing that will now bring oil companies into the scheme quickly is a prompt and firm commitment by HMG that we are going ahead regardless. Then and only will they abandon their present objectives and join in the scheme to have a say in its design and reduce BGC's influence. This commitment is needed here and now, before Parliament rises, if we are not to start incurring large and expensive delays on the physical construction side, with contracts being postponed and with a real risk that the Norwegian pipeline project will pre-empt vital supplies.

If we are unwilling to make that commitment we will inevitably have to announce soon that the project, which we have consistently backed, is no longer alive. This would cause us major political embarrassment both abroad and at home. Our hopes for associated petrochemical developments in Scotland and large orders for British industry and BSC would be lost.

In view of the extreme urgency of this decision which has been in the melting pot since I spoke to you in April, I suggest we discuss it at the earliest moment with the Prime Minister and my office will accordingly be asking hers to arrange a very early meeting.

I am copying this letter to the recipients of yours.

*Yours*

*David*

D A R HOWELL



Se Walters

Treasury Chambers, Parliament Street, SW1P 3AG

01-233 3000

13 July 1981

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

Mr Davis

GAS GATHERING PIPELINE

Thank you for your letter of 29 June which we discussed on Thursday. I certainly recognise your urgency for a decision, but it did become clear from our discussion that your proposal entailed an increase in the PSBR of at least some £1.5 billion (in January 1981 prices) over the next few years. Such an enormous increase to the PSBR is highly unwelcome on top of the other nationalised industry increases already in prospect. You argue that within a few years equity in the pipeline could be sold off to the private sector. But we cannot be certain of that, particularly in the light of our experience with the initial financing of the line, and we cannot take account of a possible sale in our public expenditure planning.

This is the background to the proposal below that there should be a further attempt to persuade the oil companies to take a majority stake in the line. But first I give my assessment of the position reached so far.

(i) The scheme agreed by E last summer was a non-starter from the outset. This was primarily because private sector investment in the integrated gas line would never be forthcoming until the gas producers were given some assurance on the price for the gas to be transported through the line. It was a mistake to have made Denis Rooke Chairman of the Organising Group. His Corporation's legitimate commercial interest is to delay giving such assurances on gas prices and to offer the minimum price.

(ii) The abolition of BGC's monopsony might in the longer run have given the oil companies the assurances on prices which they seek. But you argue that the beneficial effects of the abolition of the monopsony will take too long to come through to help with the immediate financing decision for the line. Indeed, in the short-term, the oil companies' belief that the monopsony is about to be abolished could well have discouraged them from coming to an accommodation with BGC on gas prices. The companies may also believe that the Government would never permit the line to go ahead entirely supported financially by BGC since this would have involved a massive extension of the public sector in the North Sea.

10 DOWNING STREET

Tin.

July 15, 1981.

It looks as if Energy now think the Gas-gathering Pipeline scheme is going to fall through. The latest letter seems to be setting out reasons why Treasury, and Oil Taxes, are to be blamed rather than Energy. If we are busy allocating blame for failure we must believe failure is likely!

The Government could derive great damage from this. Politically it would be made to appear that the National Interest had somehow been lost in our pursuit of Privatization. The issues are too complicated to be understood, but the impression would be left that we had failed and Norway had succeeded.

Our competence would be called into question; why are we going to throw away a lot of valuable gas?

There now appears only one solution which will result in no delay to the building program. That is the Morgan Grenfell solution, which I do not begin to understand, but which will lead to the building program and the orders for BSC and others. If the Treasury cannot grit their teeth and say, "we agree the initial financing is outside the PSBR", then we may have to explain to an unemployment battered Public that the PSBR requirements demand that the scheme does not go ahead. This could be the trigger which makes people feel certain that our economic policies are so unrelated to our present employment problems, that any change would be an improvement.

Daint.



(iii) You argue that it is impracticable to delay the start of construction of the line for, say, a year so that certain aspects of the guidelines could be relaxed, as the Prime Minister suggested in the No.10 letter of 2 July, with a view to encouraging private sector participation. This leaves the two options discussed in detail in the note prepared by our officials. They are an integrated line, which in the circumstances described in your letter would have to be financed initially with 100 per cent public sector support; or permitting the oil companies to develop the pipeline system as they themselves prefer by building new lines, adding to existing ones etc.

(iv) If the pipeline was to be built with full BGC financial support, the cheapest form of finance would be from the National Loans Fund. Bank borrowing of the type Morgan Grenfell suggest, is likely to prove more expensive.

(v) The economies of the alternative scheme - development of a multiple pipeline system by the oil companies - are soundly based, but on the figures given in the officials' paper the integrated scheme looks to have the edge. Nonetheless one has to be suspicious of jumbo projects undertaken by nationalised industries in which the private sector both banks and oil companies - have refused to take part. The multiple approach is the safer option and is one that I would certainly not rule out since it has certain advantages.

My conclusion from this assessment are that we ought to make one last try over the next few weeks to secure majority private participation in an integrated line. Such participation will not be forthcoming unless BGC can be prevailed upon to give the prospective participants some reasonably firm assurance on the price which they would be willing to pay for future gas. You will want to consider how to try to carry this forward. One possibility would be to ask someone quite independent of the oil companies and BGC to contact all the interested parties and produce an assessment of the minimum conditions each would require for participation in the line. Such an assessment would have to be prepared very quickly so that final decisions could be taken by the end of August. In the last resort there might have to be Ministerial intervention between BGC and the oil companies in order to try to hammer out an acceptable solution.

I am sending a copy of this letter to the Prime Minister, and to Robin Ibbs.

GEOFFREY HOWE





CONFIDENTIAL

Energy ltb



10 DOWNING STREET

*From the Private Secretary*

2 July, 1981

Gas Gathering Pipeline

Thank you for your letter of 29 June with which you enclosed a copy of the letter of the same date from your Secretary of State to the Chancellor of the Exchequer. I have shown this to the Prime Minister. She has commented that, on the face of it, the Government guidelines which were issued to the Organising Group were far too stringent in so far as they appear to make it extremely difficult for investing companies to make a profit on the project. She wonders whether there is any possibility at this late stage of altering the guidelines. In any case, she hopes that the difficulties which are holding up the project can be satisfactorily resolved.

I am sending copies of this letter to John Wiggins (HM Treasury), David Wright (Cabinet Office) and Gerry Spence (CPRS).

J. P. LANKESTER

R

David Lumley, Esq  
Department of Energy

CONFIDENTIAL

*at the invitation  
of Mr Wright (Ld.)  
of the Speaker (Ld.)*



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

Prime Minister

This is confirmation  
from the House that  
the only way he  
now sees the gas  
gathering ~~for~~ pipeline  
getting under-way  
is with BGC bearing  
the risks initially.  
I will let you see  
the Treasury's response.

29 June 1981

Tim Lankester Esq  
Private Secretary to the  
Prime Minister  
10 Downing Street  
London SW1

Dear Tim

GAS GATHERING PIPELINE

Your letter of 19 June recorded a meeting the Prime Minister held that day to discuss coal matters. As you know, one of the points discussed in the course of that meeting was that considerable problems were being encountered in putting together the finance for the gas gathering pipeline project. The Prime Minister, as a result, asked the Department of Energy to make renewed efforts, in consultation with the Treasury, to find a solution to the problems preventing the project from getting under way.

You may wish to see the attached copy of a letter which my Secretary of State has sent today to the Chancellor of the Exchequer and which summarises the latest position on the project.

Yours ever

*David Lumley*

DAVID LUMLEY  
Private Secretary

*TL  
22/1/7*

01 211 6402

The Rt Hon Sir Geoffrey Howe QC MP  
Chancellor of the Exchequer  
HM Treasury  
Parliament Street  
London SW1

29 June 1981

*Mc Sully*

GAS GATHERING PIPELINE

When I wrote to you on 16 April I said that the Organising Group were exploring whether companies with a potential interest in making use of the gas gathering line would be prepared to join in sponsoring its financing. But I warned that it might prove impossible to arrange financing without some form of guarantee, probably given by BGC. We discussed these points further on 28 April.

The Organising Group have duly sought private sector sponsorship of the line, concentrating now on the total financing rather than the earlier idea of interim financing which the Bank of Scotland was unable to put together. The Group have had meetings with senior executives of the key companies and now await written responses from them. But, unfortunately, it is already clear that this line of approach is getting nowhere. The companies are not prepared to take part in financing at this stage under the guidelines we laid down. A new initiative will be needed if the project is to be kept alive.

There are a number of reasons why the private companies are unwilling to invest in the pipeline at this stage. The Government guidelines issued to the Organising Group were of course intended, inter alia, to avoid the pipeline being built on the strength of tax reliefs and to prevent its effective monopoly position, once built, being exploited to yield excessive profits. These are clearly sound objectives but from the companies' point of view the consequences are:

- i) the cost of service approach in the guidelines means that if things go better than expected the benefits will go to those who pay the transmission tariffs, which would be lower, rather than to those who invested in the line;
- ii) the separation of the pipeline company from field development, as opposed to the joint venture approach, means that there is no strong tax incentive for any individual gas producer to join. As a group, producers do need the project. But a perfectly rational strategy for them, particularly for those with fields not due to produce gas in the early years of the pipeline's operation, is to sit back and let someone else bear the construction risks.

Then there is the physical design of the project. Some producers would like to undermine the integrated gas gathering concept so as to eliminate the risk of competition to their own pipelines. Naturally enough they are not concerned with the effect of that on fields owned by other companies, or on national gas supplies. Shell/Esso have proposed an alternative scheme based on several separate offshore pipelines and greater use of the FLAGS system which they own. Not only do we have strong reservations about the physical aspects of their proposals, but the central multi-user gathering line proposed in their scheme would still involve the same financing problems we are struggling with now. Shell/Esso have said that they would not contribute to sponsoring it.

Lastly there is the issue of gas prices. Knowing that we are seeking their financing support the producers naturally see a chance to exact high price terms. Most talk about crude oil parity, or a fraction of that not much less than 100%. BP have told us that for much of their gas they will be looking for prices equivalent to the highest paid internationally. Mobil are refusing to conclude a deal with BGC (which BGC thought to have been agreed in principle more than once during the negotiations) for associated gas which costs almost nothing to produce and for which BGC has offered some 16p/therm. Major price concessions would cause us embarrassment internationally at a time when we and other IEA or EC countries have been seeking to resist moves by producers (Algeria, Norway) to charge oil-related prices. More important they would be a drain on our national economy and raise prices to UK industry and domestic consumers.

All these points have featured in the Organising Group's discussions with the producers. Their written responses, including those from BP and Mobil, will inevitably ask for concessions on taxation, gas prices and project incentives as conditions for their backing the integrated gas gathering scheme. Even if we could eventually negotiate our way through those demands, which is in my judgment unlikely, the delay in doing so would undermine the present timetable. The joint BP/Mobil/BGC venture which is currently paying the costs of keeping the project on track expires at the end of July and there is no chance of the companies extending it beyond that date. At the same time major expenditure on the St Fergus terminal needs to be committed this Summer. If the project is now delayed the

momentum will be lost and the integrated scheme would almost certainly collapse. Its replacement would be a few piecemeal developments (elements of which are recommended by Shell, Esso and the French) which would be much less favourable in national economic terms, and which would be largely built at the taxpayers' expense. Gas supplies would be delayed or lost and our hopes for petrochemical development based on the pipeline would probably have to be abandoned.

Despite the financing difficulties, the project remains highly economic. There is an overwhelming case for a gas gathering system - the discounted value of the gas and liquids which would be landed by the £1½ billion line is some £25 billion at today's prices. Investment in the pipeline has to be considered in the context of investment in the North Sea which has a history of extremely high profitability, rather than in terms of the projects with more dismal outcomes normally associated with the public sector. Even the most favourable pattern of piecemeal developments would certainly be less economic than the integrated scheme and could be seriously worse to the extent that it failed to collect all the gas reserves for which the integrated scheme is designed. What is more, such developments would be financed to a major extent by tax reliefs. The validity of the comparison has been tested against a number of alternative assumptions.

We therefore need to decide well before the end of July where the finance is coming from if we are not to lose the chance of building the most economic and nationally favourable gas gathering scheme. The only feasible way now to keep the integrated scheme going is for BGC to bear the risks initially. Morgan Grenfell have produced a fallback financing package which would keep the project alive and on timetable by BGC starting it off. Their and our expectation is that some of the producers would eventually join in to maintain their influence, and that other private sector money would come forward when the risks had visibly diminished. This is allowed for in the structure of the proposal and would get us back to our agreed objectives and to the form of pipeline company we want. I am certainly not wedded to the details of the Morgan Grenfell scheme, but if we do not pursue this option or some other way of BGC taking the initial risk we face the strong probability that the project will disintegrate, despite its economic sense.

One other point I should mention on this is the change we are now proposing to make in BGC's gas purchasing monopoly. I have recently told Sir Denis Rooke formally of our intentions and he has pointed out that his Board agreed in principle to the idea of BGC underwriting the scheme initially only on the basis that their gas purchasing privileges would be retained. I do not believe that this is an insurmountable problem. BGC are relying on the gathering line gas to meet their market commitments and, whatever the change in their monopoly position, will inevitably buy quite a lot of it when the time comes. For these reasons I hope to be able to persuade them to set aside their reservations and will if necessary argue the point with the full Board.

Your officials already have the details of the BGC/Morgan Grenfell proposal and we have agreed figures with them which show a strong economic case for going ahead with the integrated scheme. We now need to decide quickly whether, as I believe is fully justified, BGC should be authorised to take the initial risks. We have openly committed ourselves to giving the integrated gas gathering scheme the full backing of Government. If we now decide against proceeding with the scheme because the initial risks have to be borne by BGC, I believe that we shall attract severe criticism not only from the Opposition but also from our own supporters. We can also expect to see piecemeal schemes emerge which would be less economic and could be less favourable for the PSBR. I should be most grateful for an early meeting with a view to reaching a decision as early as possible in July.

*Yours*  
*Howell*

D A R HOWELL

2.

Prime Minister:

possible problems ahead  
over the financing of the  
pipeline.

~~SECRET~~

~~SECRET~~

14/4  
24.4

SECRETARY OF STATE FOR ENERGY  
10, WHITE HALL, LONDON, SW1A 2JH

01-211-6402

*mt*

*Energy*  
*D*

The Rt Hon Sir Geoffrey Howe QC MP  
Chancellor of the Exchequer  
Treasury Chambers  
Parliament Street  
London SW1

16 April 1981

*Dear Sir*

GAS GATHERING PIPELINE

Our officials have, as you know, been discussing the position which is emerging on the financing of this project. Work so far has been financed under a joint venture agreement between BGC, Mobil and BP.

The original aim, as you know, was that the pipeline company of the structure we agreed at 'E' last year should be in place by the end of 1980. The Organising Group (BGC, BP and Mobil) however advised in the light of both merchant banking advice (Morgan Grenfell) and that of Sir Jasper Hollom, that it would not be possible to move to the fully fledged company until sufficient throughput contracts had been concluded with the producers of the gas. They therefore recommended that an interim company should be set up which would raise the finance and take the construction forward until the end of 1983 when it was expected that sufficient throughput contracts would be in place to allow the final company to be formed. The aim was that this interim company could be set up by 1 April but the arrangements for financing it have run into some difficulty.

The Bank of Scotland originally suggested that they together with a consortium of other banks (Lloyds, Barclays, Nat West, Morgan Guaranty and Citibank) would be able to put up £700m of interim finance without any Government guarantee. They sought only certain assurances (which we do not think present difficulty) about the exercise of our depletion policies. On closer examination of the project, however, they are now concerned that the number of gas-fields which have so far received development approval (known as Annex B)

is smaller than they had expected and they are now seeking either from HMG or the sponsors of the project some form of security or guarantee that, once their loan of £700m has been spent, further finance will be forthcoming from elsewhere to complete the project and so repay their loan. Their position is that they can regard as "bankable" only that gas expected to come from fields which already have Annex B development approval; and that, while those quantities of gas might support bank lending of about £700m, they would not support lending of the entire project costs. The Banks will not accept the risk that, should the expected long term finance not materialise by the end of the interim period, they would have to lend the remaining finance to complete the line in order that the bankable gas could flow and repay their £700m interim loan.

On the Bank of Scotland proposal there would be no immediate requirement on HMG or BGC to put up any cash; the contingent liability to provide completion finance would not arise until 1 January 1984 or until the interim loan had been expended, if earlier. In the next couple of years we can expect a number of further fields to get Annex B approval and a number of through-put contracts to be negotiated. We are essentially therefore talking about bridging finance and the chances of the contingent liability being called are in my judgement small. Once this 'bridge' is crossed the project remains highly attractive, (the present calculations assume a real rate of return of 5% to equity holders; the total value of the gas recovered from fields with, or about to receive, Annex B development approval will be some £13½ billion at a conservative gas valuation).

The Organising Group will be having further discussions with the Bank of Scotland, and they are also exploring with oil and petrochemical companies who have an interest in seeing the line proceed whether they would be prepared at this stage to join in the sponsorship of the Line. Whether however we go down the Bank of Scotland route or some other approach, it could well prove impossible to arrange the financing required without some form of guarantee by HMG, or preferably by BGC. The specific form this might take cannot yet be formulated. But I thought I should give you this early warning that some form of guarantee is likely to be necessary.

We cannot afford to allow the project to falter. Any delay would, in my judgement, cause the present scheme to collapse with serious consequences for gas supplies. There would be a shortfall between BGC's foreseen supply and demand which could not readily be met by other sources. It would also mean that the opportunities for using natural gas liquids to strengthen the petrochemical industry would be diminished. I would therefore appreciate an early discussion with you to explore how we might handle the problem. I recognise that, when we are clearer about what might be involved, a collective discussion with our colleagues will be necessary.



3

I am sending a copy of this letter to the Prime Minister and to Sir Robert Armstrong.

*Howell*

D A R HOWELL

*David*



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

01-211 6402

Tim Lankester Esq  
 10 Downing Street  
 London SW1

*Energy*

2

PRIME MINISTER

A more detailed  
 report, foreshadowing  
 public (guarantee)

involvement in financing  
 the pipeline.

3 April 1981 MS

3/4

Dear Tim,

*ms*

GAS GATHERING PIPELINE

I attach the note on the gas gathering pipeline that you requested for the Prime Minister, following the "North Sea pipeline plan shelved" article in the Financial Times on 1 April. Following your letter of 6th January we were anyway about to put forward a quarterly progress report on the project; the attached note will, I hope, serve that purpose also.

Technical progress remains good but there are problems in financing. We would therefore draw the Prime Minister's attention to paragraph 11 of the note — *and para 12!*

MS

~~Yours ever,~~

J D WEST

Enc



## GAS GATHERING PIPELINES

## PROGRESS REPORT FOR THE PRIME MINISTER

Introduction

- 1 A year ago a BGC/Mobil study reported in favour of a new gas gathering pipeline in the northern North Sea (see attached map). The study was made public in June, and the Secretary of State for Energy, following a decision by "E", announced that the Government considered a pipeline system along the general lines recommended would be in the national interest and should be constructed as quickly as possible. He' announced the formation of an Organising Group comprising BGC, MBP and Mobil to develop proposals for a private utility transmission company outside the public sector to build and operate the line. It was envisaged that BGC would hold 30% of the equity, the remainder being offered to financial institutions, licensees, customers for the natural gas liquids (NGL) and perhaps the general public; the pipeline company would be financed substantially by loan finance raised from the markets, and without Government guarantee.

Technical Work

- 2 The Organising Group is making good progress on technical work:
  - offshore BP has completed conceptual design work on the pipeline itself; surveys of the pipeline route are in hand. BP are in close touch with British Steel as the final specification for pipe emerges. While the tight timetable will prevent the entire order being placed with one supplier, the Organising Group is well aware of our hope that British Steel could win the major part of the work.
  - for the St Fergus terminal, land has been acquired, planning permission obtained, and conceptual design completed. Work

is now in hand on prequalification of contractors who might be invited to tender for the construction contract.

- although the final onshore disposal pattern for NGL will not be clear until commercial negotiations are complete (see para 7), the Organising Group is advancing planning for facilities which may be required.

#### Completion Target Date

- 3 The original target date mentioned in the Secretary of State's June announcement was 1984/85. In the light of the detailed engineering design work now completed the Organising Group has now adopted 1985 as its target. As expected, the critical item is not the offshore pipeline itself but the St Fergus terminal.

#### Gas Availability

- 4 The Organising Group after consulting the field operators has updated the gas availability figures used in the BGC/Mobil study. The results show gas availability at least as high as in the previous figures. For the critical early years this result depends on including gas from North Alwyn, whose licensees (Total and Elf) are now preparing to seek development approval. Total and Elf wish to put North Alwyn gas into their Frigg pipelines, but this would involve a 110 km pipeline duplicating part of the gas gathering pipeline's route. We are pressing them to commit North Alwyn gas to the gas gathering line; meanwhile we are holding back award of Seventh Round licences for which they had applied.

#### Norwegian Gas

- 5 There had been hopes of attracting into the line Norway's 84% share of gas from the Statfjord field, and BGC put in a fully competitive purchase offer. However the Norwegian Government has recently decided that the gas should be landed in Norway (political pressure to land hydrocarbons in Norway for the first time is immense). Norwegian Statfjord gas would have helped the UK line reach full utilisation more

quickly. But its loss is not critical - the line is economic on the basis of UK gas alone, and we have made clear that the UK share of Statfjord gas will be coming to the UK.

#### Costs

- 6 The detailed engineering design work now completed has produced a revised cost estimate of £1.5 billion at January 1981 prices. This compares with the original estimate in the BGC/Mobil study of over £1.2 billion on the same price basis. £150m of the increase is accounted for by the inclusion of a new item, an ethane pipeline from St Fergus to Teesside which could be constructed if the final NGL disposal pattern so required.

#### NGL Disposal Onshore

- 7 The NGL which the line will bring ashore has considerable potential as a petrochemical feedstock and a number of companies are seeking supplies to feed new plant or improve the economics of existing plant. To identify a major seller with whom these companies can negotiate and get the disposal arrangements settled speedily BNOG and BGC have, at the Secretary of State's invitation, formed a joint venture to market those NGLs which will fall to the public sector (notably as a result of BNOG's participation rights). Negotiations are now beginning. The uncertainty meanwhile as to the final disposal pattern does not threaten delay; if the offshore line and St Fergus are ready to accept gas before final NGL facilities are completed, interim NGL outlets are possible.

#### Southern Leg

- 8 The BGC/Mobil study envisaged the southern leg of the line running as far south as the Fulmar field. Shell/Esso subsequently suggested that much more gas might be available in the southern area, so that a separate line to shore might be needed. The Organising Group decided to defer a decision on how best to collect gas south of Lomond until further exploration had given a better picture of the gas likely to be available. A garbled report in the Financial Times on 1 April presented this as in some way a step back. It is not. In fact it permits a better informed decision and does not delay the main line.

Financing

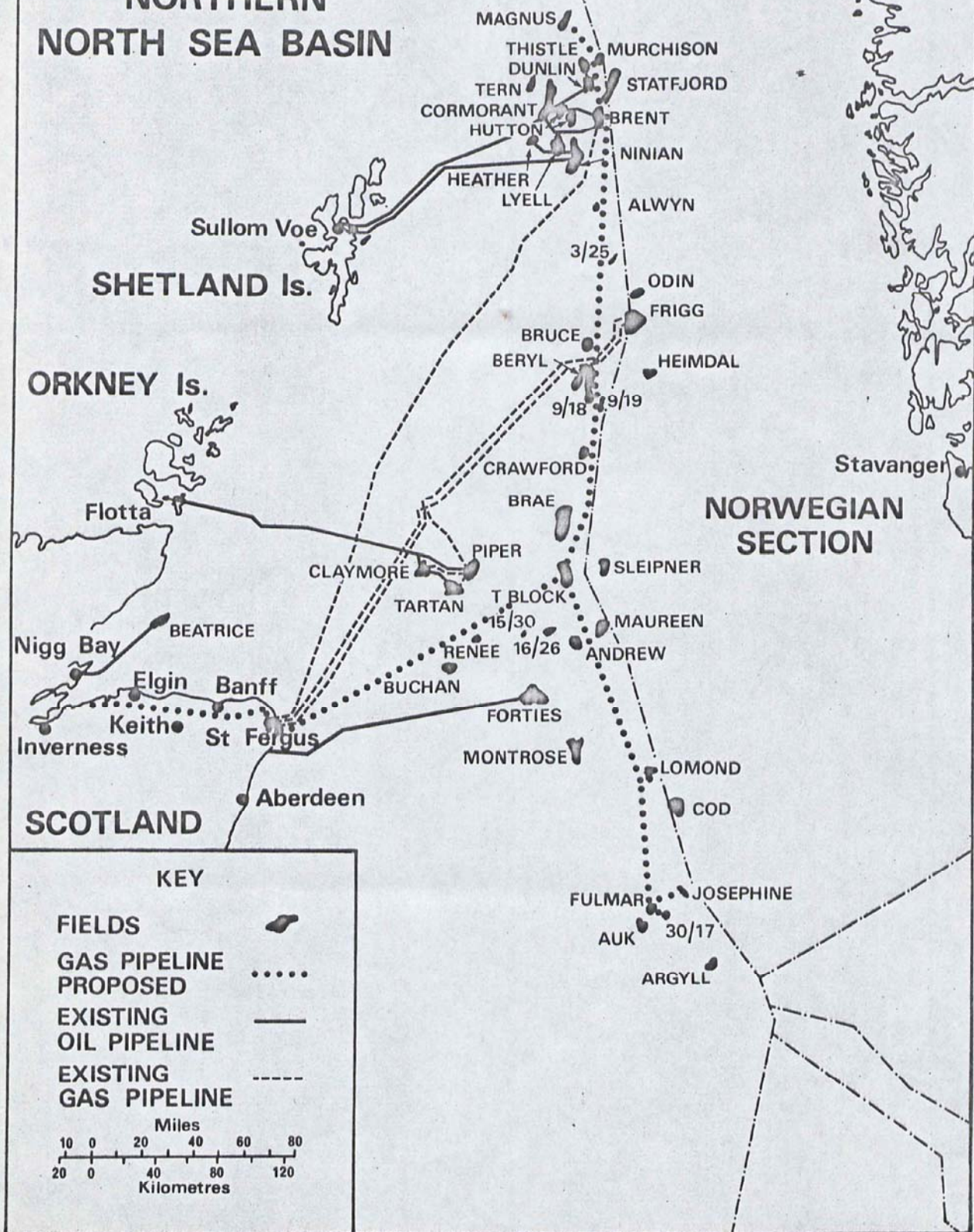
- 9 This is currently the biggest challenge facing the Organising Group and their financial adviser, Sir Jasper Hollom (formerly Deputy Governor of the Bank of England). Financing discussions are not however holding back technical work, because the Organising Group itself is providing the necessary funds - over £8m has already been committed.
- 10 The long term objective is to raise project finance secured on gas throughput contracts, and to involve a wide range of equity holders as envisaged by the Secretary of State. By last autumn the Organising Group had concluded that an interim company would be required to undertake the initial stages of the project - merchant bank advice was that potential public and institutional shareholders would at this stage perceive the risks as too great and the prospect of reward as too distant. The Organising Group set itself the target of forming an interim company by 31 March. The Bank of Scotland then suggested that banks might provide interim finance, and formed a study group comprising Barclays, Lloyds, National Westminster, Morgan Guaranty and Citibank to examine the project in detail. In mid-March the banks submitted a modified idea: interim bank lending would require not only non-financial assurances on exercise of Government powers over North Sea development (where we believe we can meet banks' needs) but also a completion undertaking to take effect if the expected long-term finance did not materialise. This latter requirement arises because a main purpose of the integrated gas gathering line is to serve fields not yet under development, whereas banks are prepared to lend project finance only on gas from fields already under development. Those fields under development today do not have enough gas to support bank lending of the entire project cost. There is thus a gap which will decline through time as more fields begin development but which initially must be covered by some other contingent security, to be invoked if new field developments are not in step with financing needs.
- 11 The Banks, led by the Bank of Scotland, (unlike the City) have shown imagination in their approach to this problem and the guarantees they are seeking are not unreasonable. This is also the view of the Governor
-

of the Bank of England with whom the Secretary of State had discussed the problem. The Organising Group are discussing with the Banks the various means by which credit-worthy shareholders in the interim company could provide a satisfactory guarantee or security. Potential shareholders are the present members of the Organising Group (BGC, BP, Mobil) and other oil companies, and perhaps companies seeking larger supplies of NGLs from the line.

12 However, it is vital that the project should not be delayed and we must now face the fact that sufficient support may not be mustered in time. To bridge this 'time gap' there is probably no alternative to some kind of limited - and reducing - guarantee or security being given either by HMG or preferably BGC (with Government approval). Officials have therefore been instructed to discuss with the Treasury the probable need for BGC to provide the sort of guarantee indicated. The chances of it being called are on present estimates small. An early paper will be submitted to Ministers.

---

# NORTHERN NORTH SEA BASIN







Energy

Treasury Chambers, Parliament Street, SW1P 3AG

Rt Hon Sir Keith Joseph MP  
Secretary of State  
Department of Industry  
Ashdown House  
123 Victoria Street  
London SW1

23 January 1981

*R. King*

*not correct  
will obtain  
agreement*

GAS GATHERING PIPELINE AND DISPOSAL OF NATURAL GAS LIQUIDS

Thank you for your letter of 9 January..

I note your views about the value of any study of pricing before the bids have been put in, but I think it as well that we consider in advance the likely problems that may arise if the bids go one way rather than another. In your letter, you say that you foresee one such problem - the effect on the petrochemical industry if the price of ethane is forced up by the producers. It may well be that the price will not be beyond the reach of the petrochemical industry: the total supply of ethane is, I understand, expected to be more than BP, Shell, Esso and ICI can take; other potential bidders may drop out and the supply will be increased as more fields are linked to the gas gathering system after the mid-1980s. In any case, not much of the benefit will go to the producers, since about 90% of the incremental profit will be taken through the tax system.

I am sending copies of this letter to members of E Committee, to George Younger, Francis Pym and Sir Robert Armstrong.

*Law*  
*can*

LEON BRITTAN



SECRETARY OF STATE FOR ENERGY

THAMES HOUSE SOUTH  
MILLBANK LONDON SW1P 4QJ

01-211-6402

*Energy*

1. *Tim*  
To see

2. *AK*  
*AKS*  
*131*

Clive Whitmore Esq  
Principal Private Secretary  
10 Downing Street  
London SW1

13 January 1981

*Dear Clive,*

GAS GATHERING PIPELINE

Thank you for your letter of 6 January. We have arranged for the requested quarterly reports on progress to be produced, and you can expect the first one for the period to end March.

*Yours ever,*

J WEST  
Private Secretary

*Energy* *July 79*



cc Mr Duguid

10 DOWNING STREET

From the Principal Private Secretary

6 January 1981

BF 6.4.81

Dear John,

6.7.81

GAS GATHERING PIPELINE

6.10.81

etc.

You will recall that you wrote to Tim Lankester on 2 December 1980 about Mr. Eldon Griffiths' letter of 30 October to the Prime Minister about the gas gathering pipeline. The Prime Minister replied to Mr. Griffiths' letter on 8 December on the lines of the draft attached to your letter.

The Prime Minister has recently been re-reading this correspondence. She remains concerned about the prospects for completing the pipeline on time and she would be grateful if your Secretary of State could let her have a quarterly report on progress.

Yours now,

Alvi Whitman.

J.D. West, Esq.,  
Department of Energy.

98

CONFIDENTIAL

PRIME MINISTER

GAS GATHERING PIPELINE

You saw over the Christmas holiday a secret report which said that the Norwegian Government's doubts about whether the British gas gathering pipeline would be completed on time had not been allayed by their recent discussions with Mr. Howell, and you said that we should enquire about the prospects for the completion of the pipeline.

Because of its sensitive nature the secret report has not been copied to the Department of Energy, and we would therefore be unable to relate your enquiry about the completion of the pipeline to it. As it happens, we had the attached letter from the Department of Energy about the pipeline as recently as the beginning of this month (flag A). You saw this at the time. The letter reports that the Organising Group is making progress and is still of the view that the target date of 1984/85 for the completion of the pipeline should be achieved. The letter refuted in particular Mr. Eldon Griffiths' suggestion that the pipeline was being delayed because of a lack of private finance and that the stumbling block was BGC's unwillingness to offer prices acceptable to North Sea producers. You may also like to be reminded of what you said when you wrote to Mr. Griffiths (flag B).

Are you content with this account of progress on the pipeline or would you like us to make further enquiries about the timetable for its completion?

KHW.

29 December 1980

We will keep a particularly close watch on events and ask for a quarterly progress report.

CONFIDENTIAL

MB.

500 NIS Energy



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

Tim to see

+PA

MS

17/12

~~cc Mr Ingham~~

Nick Sanders Esq  
Private Secretary to the Prime Minister  
10 Downing Street  
London SW1

17 December 1980

Dear Nick,

Tim Lankester's letter to me of yesterday conveyed the Prime Minister's agreement to my Secretary of State's announcing the Government's views on NGL disposal from the gas gathering pipeline by a written answer today.

I attach for information a copy of the final text, incorporating the change requested by the Chief Secretary and some minor drafting changes.

I am copying this letter to Ian Ellison (Industry), Godfrey Robson (Scotland) and Terry Matthews (Treasury).

Yours ever,

J D WEST  
Private Secretary



DRAFT PUBLIC STATEMENT

Valuable natural gas liquids will be brought ashore by the new Gas Gathering Pipeline. The ethane, in particular, will be an important new feedstock for petrochemical plants in the UK. Timely completion of the facilities for handling these natural gas liquids is essential to the gas gathering system as a whole.

The Organising Group I set up in June has just made recommendations to me on the handling of these hydrocarbons. Their advice is that the ethane should be extracted at St Fergus and piped separately to users, with the processing of the remaining stream carried out at Nigg Bay. They recommend that preparatory work should be carried out on an ethane line from St Fergus to Mossmorran and, Grangemouth, with an extension to Teesside, and that an ethane line from St Fergus to Nigg Bay should also be considered. The Organising Group has stressed the urgent need for decisions on the routing of the NGLs. They have invited me to decide how they should be aggregated into quantities sufficient for bulk contracts to be entered into for petrochemical use.

I have invited the Organising Group to develop their planning on the lines recommended.

It is, however, my view that the actual pattern of disposal of the NGLs should be determined by commercial negotiations. At least seven companies have expressed an interest in purchasing

/the ethane

the ethane as feedstock for petrochemical manufacture and several licensees have expressed a need for reassurance that they will be able to regain access to natural gas liquids after onshore fractionation into component products. It is important that commercial negotiations for the sale and processing of NGLs should proceed quickly to a point which enables the pattern of onshore disposal to be settled. To facilitate this, clarity is needed on the rights and roles of the various parties with an interest in the system. I have therefore today confirmed to the British National Oil Corporation that I shall not stand in the way of the exercise by the Corporation of the rights to natural gas liquids which it enjoys under participation agreements. The British National Oil Corporation and the British Gas Corporation have informed me that they will co-operate in the disposal arrangements, as appropriate. These developments identify to prospective purchasers a substantial seller able to enter promptly into disposal negotiations. Taken together with the Organising Group's work on the processing arrangements, this should enable the pattern of the onshore facilities to be determined. There will be no obligation on licensees to sell the remainder of their natural gas liquids through an intermediate agency.

I have invited the Corporations and the Organising Group to seek to maximise the national economic benefit and as part of this to recognise the importance of petrochemical activity in the UK based on natural gas liquids. I have asked them to ensure, so far as possible, that facilities to process the NGLs, including any extracted from Norwegian gas if it becomes available, will be provided in accordance with the timetable envisaged for the gas gathering pipeline as a whole. They are

/to ensure

to ensure that, subject to participation, licensees can recover their own material after fractionation and that later licensees and customers have access to the system on reasonable terms. I have made it clear that BNOC should not commit itself to investment in petrochemical plant.

I expect all parties to the commercial negotiations to conduct them constructively and speedily. It would not be acceptable for any of the parties to block agreement on reasonable terms if this threatened to impede timely completion of the Gas Gathering system.



*Energy*

Tel: 211 6402

Rt Hon John Biffen MP  
Chief Secretary  
Treasury Chambers  
Parliament Street  
London SW1

*R.M.*

17 December 1980

THE GAS GATHERING PIPELINE AND DISPOSAL OF NATURAL GAS LIQUIDS

Thank you for your letter of 15 December. I have taken on board your proposed amendment to the announcement.

you  
I can assure that there is no question in my proposals of subsidised or below market feedstock prices for the petrochemical industry. I am also very willing to reconsider the preferred strategy of disposing of the ethane to the Four should Dow prove willing to offer better terms for it. I should not, however, wish to look at prices alone irrespective of the other terms offered by the competitors for the ethane, the effects on the reliability of the gas gathering system and the total amount of ethane channeled into petrochemical use.

Hamish will be writing separately to you on tax and public expenditure.

Finally I have asked my officials to consult Treasury and Inland Revenue officials on the guidance which I propose to give ENOC.

*Hamish*  
*David*

D A R HOWELL

CONFIDENTIAL



10 DOWNING STREET

From the Private Secretary

cc HO PGO  
FCO CDL  
HMT SO  
D/I  
LPO Energy  
D/EMP bcc Ingham  
MAFF  
D/T  
CSO  
CO

16 December 1980

BF for Hansard

Gas Gathering Pipeline and Disposal of Natural Gas Liquids

The Prime Minister has considered your Secretary of State's minute of 9 December, the Secretary of State for Industry's minute of 15 December, and also the Chief Secretary's letter of 15 December.

This is to confirm that the Prime Minister is content with Mr. Howell's proposals, and that he should make a statement on the lines of the draft attached to his minute, subject to the amendment proposed by the Chief Secretary at the beginning of paragraph 5. She also accepts that this statement can be made by Written Answer tomorrow (Wednesday).

I am sending copies of this letter to the Private Secretaries to the members of E, Godfrey Robson (Scottish Office), Robin Birch (Chancellor of the Duchy of Lancaster's Office), Richard Prescott (Paymaster General's Office) and David Wright (Cabinet Office).

TP2

J.D. West, Esq.,  
Department of Energy.

CONFIDENTIAL

Energy July 79  
with RL



SCOTTISH OFFICE  
WHITEHALL, LONDON SW1A 2AU

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

MBM

RL

16 December 1980

16/12

Dear Secretary of State,

GAS GATHERING LINE

Thank you for copying to me your minute of 9 December to the Prime Minister about the gas gathering line and disposal of natural gas liquids.

I agree that your minute reflects the discussion which we had last Thursday and I am broadly content with the draft statement. There are however two respects in which I think it might be helpful to expand it slightly in the interests of clarification. They are as follows.

First, as I mentioned at our meeting I think it would be useful if the statement made clear that the work of the Organising Group would be continuing. A simple amendment to the first sentence of paragraph 2 along the lines of "The work of the Organising Group which I set up in June is continuing. Meanwhile the Group has just made recommendations to me on the handling of the gas liquids", would I suggest, suffice.

Secondly the statement makes no reference to the Occidental proposal. This is understandable since it is not embraced by either of the pipeline options. Nevertheless its omission might be misconstrued. I think therefore that there would be merit in detailing at paragraph 4 the "seven companies" in alphabetical order - BP, Dow, Esso, Highland Hydrocarbons, ICI, Occidental and Shell - who have expressed an interest. This would also help to confirm the impression that all the companies are still in the running.

I am copying this letter to the Prime Minister and to the recipients of your minute.

Yours sincerely,

J.S. Wilson

Approved by the Secretary  
of State and signed in his  
absence.



Treasury Chambers, Parliament Street, SW1P 3AG

Rt Hon Sir Keith Joseph Bt MP  
 Secretary of State  
 Department of Industry  
 Ashdown House  
 123 Victoria Street  
 London SW1

16 December 1980

*Dear Secretary of State,*

*TPM  
19/12*

GAS GATHERING PIPELINE AND DISPOSAL OF NATURAL GAS LIQUIDS

I have seen your minute of 15 December to the Prime Minister commenting on David Howell's of <sup>TPM</sup> 19 December about his approach to the disposal of natural gas liquids (NGLs) from the gas gathering pipeline. You will no doubt have seen my letter of 15 December in which I said that I did not dissent from David Howell's general approach provided I could have his assurance that there is nothing in it which would commit us to a policy of prices for feedstock for the petro-chemical industry which were below market levels. This could jeopardise Government tax take from the North Sea if the consequence was for a lower reference value for PRT etc purposes. In order to avoid any impression that we were contemplating a policy of prices below market levels, I asked that the first sentence of the fifth paragraph of the proposed statement should be revised to read:

"I have invited the Corporation and the organising group to seek in these negotiations to maximise the national economic benefit and as part of this to recognise the importance of petro-chemical activity in the UK based on ethane."

You will see from this why I am concerned to read your minute which might be interpreted as arguing that the petro-chemical industry should receive the feedstock at below market prices. As I explained in my letter to David Howell, this could jeopardise Government tax take from the North Sea and very substantial amounts of revenue could be at stake. I cannot therefore accept that it would be short-sighted to obtain proper market prices for the feedstock. I must therefore reserve my position on the matter on the prices to be charged for the feedstock and the consequent tax take.

I do not think that this need delay David Howell's statement if he and other colleagues are content with the drafting amendment which I suggested above. But I suggest that Treasury, Inland Revenue, Industry and Energy officials should prepare a note for us on pricing and the associated tax implications of the disposal of the feedstock. This note should cover the points, among others, in the second half of my letter of 15 December to Hamish Gray, a copy of which I attach.

...  
I am sending a copy of this letter to the members of E Committee, George Younger, Norman St John-Stevas, Angus Maude and Sir Robert Armstrong.

*Yours sincerely*

*T. Matthews*

*for* JOHN BIFFEN

[Approved by the Chief Secretary  
and signed in his absence]



cc Chancellor of the Exch.  
Financial Secretary  
Minister of State (C)  
Minister of State (L)  
Sir D Wass  
Mr Ryrice  
Mr Dixon  
Mr Burgner  
Mr G P Smith  
Mr Wicks

Mr Thornton  
Mr Ridley

Treasury Chambers, Parliament Street, SW1P 3AG

PS/IR  
Mr Whitehead  
PS/C&E

Hamish Gray Esq MP  
Minister of State  
Department of Energy  
Thames House South  
Millbank  
London SW1

15 December 1980

*Dear Minister,*

*R  
14/12*

THE GAS GATHERING PIPELINE AND THE DISPOSAL OF NATURAL GAS LIQUIDS

Thank you for your letter of 9 December about the public expenditure and tax consequences of David Howell's proposals in his minute of 9 December to the Prime Minister. Perhaps I could take these two aspects in turn.

I am glad to note from your letter of 9 December that David Howell's proposals concern only the ownership of the NGLs and the negotiations for their disposal and that they do not concern ownership of or investment in the physical facilities for transporting and processing the NGLs. That is for later decision. I also note that in his statement he makes it clear that BNOC should not commit itself to investment in petro-chemical plant. I assume from this that his proposals therefore involve no addition to either BNOC or BGC's capital expenditure programmes.

Public expenditure might also be involved if BNOC was financially exposed through the proposed trading arrangements for the NGLs. As you recognised in your letter, there might be a possibility that BNOC would accept a long-term price for the ethane, but would be forced by the provisions for independent arbitration in its participation agreements to pay a higher price to the licensee. Such a mismatch of buying and selling prices could drive the Corporation into substantial loss and therefore increase public expenditure. The risk here is increased by the fact that BNOC will have to negotiate contracts with its customers for the sale of the ethane long before it exercises its participation rights.

You suggest that this difficulty can be overcome by making the price formulae in BNOC's sale contracts to its customers contingent on the Corporation's being able to negotiate appropriate understandings with the licensees in elaboration of the present participation arrangements. I am sure that some arrangement on

these lines is essential if the Corporation is to avoid locking itself into a long-term contract for the sale of the NGLs at a specified price which would be lower than the price it has to pay under the participation agreements for the NGLs. Some tricky negotiations will be needed to avoid this risk and the Corporation will need to ensure that it has staff well experienced in NGL trading. I am not sure that they have yet recruited staff with this experience.

#### Tax

I am glad to see from your letter that you share my concern about the need to maximise the yield of oil taxation. As you say, this requires the licensees to retain ownership of the NGLs until after fractionation. Every effort should be made to meet this objective when establishing the arrangements under which NGLs will be supplied and sold. Indeed, it should be reflected in the guidelines which you propose to give BNOC.

I also note your belief that the wider role proposed for BNOC might assist Inland Revenue in ensuring proper valuation of ethane streams for tax purposes. Certainly there are few reliable analogues which the Inland Revenue can use in arriving at the market value of ethane in non-arms length deals. Nevertheless, I would not place as much emphasis as you do on the advantages of BNOC's exercise of participation rights in this respect. After all, BNOC's equity interests will automatically give it a substantial quantity of ethane - and the prices fetched for this would in any case help to serve as a cross-check where ethane has to be valued for tax purposes. It does not therefore follow that BNOC's role as wholesaler would significantly increase our ability to maximise tax receipts arising from NGL sales.

There is, however, one way in which such participation might adversely affect our tax receipts. If BNOC's participation agreements were written so that their purchase of the NGL stream occurred before fractionation, the valuation of the NGL stream for PRT etc would be based on the pre-fractionation value of the material sold to BNOC, ie excluding the added value from fractionation. This would evidently frustrate the objective outlined in paragraph 5 above. My officials understand from yours that the Corporation's participation rights are generally exercisable upon the fractionated stream so that the problem should not arise. But if this is not the case, I must reserve my position on the exercise of participation rights in circumstances where tax revenues might be significantly affected.

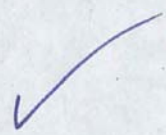
*Yours sincerely*  
*T. Matthews*

*for* JOHN BIFFEN

[Approved by the Chief Secretary  
and signed in his absence]

CONFIDENTIAL

Gas gathering pipeline  
Energy July 79  
TL over Wle



Treasury Chambers, Parliament Street, SW1P 3AG

Rt Hon David Howell MP  
Secretary of State  
Department of Energy  
Thames House South  
Millbank  
London SW1

15 December 1980

Dear Secretary of State,

THE GAS GATHERING PIPELINE AND DISPOSAL OF NATURAL GAS LIQUIDS

I have seen a copy of your minute of 9 December to the Prime Minister seeking approval for the terms of a public statement about the handling of the natural gas liquids (NGLs) which will be extracted at St Fergus from the natural gas from the gas gathering pipeline (GGP).

The General Approach

First, let me say that I assume that the NGL disposal pattern which you want to achieve is for the ethane to be piped south for use by Shell, Esso, BO and ICI - the Four - at their existing and projected plants at Moss Moran, Grangemouth and Teeside, with the remainder of the NGL stream being fractionated at Nigg. Your judgement, and that of Keith Joseph and George Younger is, I understand, that it is better to support existing and projected petro-chemical activity at these three sites rather than encourage Dow to build a new ethane-based development at Nigg. The Four's present petro-chemical operations are in the doldrums and it is believed that a secure supply of feedstock from the GGP would underwrite their operations in the UK for many years.

I do not question this judgement of industrial policy, but I am somewhat concerned with the various references in your minute and in the proposed public statement which could be taken as an indication that ethane and the other NGLs would be made available to the petro-chemical companies at artificially low prices. For example, you say at (ii) in the second paragraph of your letter that one of the objectives should be "to make as much ethane as possible available to the British chemical industry at the most advantageous terms". And the first sentence of the fifth paragraph of the proposed statement reads:

1.

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"I have invited the Corporation [BNOC] and the organising group [for the gas gathering pipeline] to seek in these negotiations to maximise petro-chemical activity in the UK based on ethane."

I think that the Treasury would need a good deal of persuading before agreeing that we should embark on a policy of subsidised feedstock prices for the petro-chemical industry. This could jeopardise Government tax take from the North Sea (about which I have written separately to Hamish Gray) if the consequence was for a lower reference value for PRT etc purposes. This problem of subsidy would presumably be raised in acute form if Dow were ready to outbid the Four for the ethane. We might then face a real dilemma. A sale to the Four would be harder to justify on economic grounds and might reduce tax take from the North Sea.

However, I do not dissent from your general approach provided I can have your assurance that there is nothing in it which would commit us to a policy of prices for feedstock for the petro-chemical industry which were below market levels. In order to avoid any impression that this is the case, I should like the sentence quoted above from the statement to be revised to read:

"I have invited the Corporation and the organising group to seek in these negotiations to maximise the national economic benefit and as part of this to recognise the importance of petro-chemical activity in the UK based on ethane."

Could I also ask that your preferred strategy of disposing of the ethane to the Four should be reconsidered if Dow prove willing to offer a higher price for it.

#### BNOC's Involvement

I recognise the need for a "wholesaler" in this operation to act as an intermediary between the petro-chemical customers and the 40 or so licensees with NGLs to sell. Negotiations between each licensee and all the prospective customers would indeed be very protracted and would risk the timetable for the whole GGP project. Nevertheless, I am, like you, somewhat hesitant about giving the state corporation, BNOC, such a central role in the arrangements for the disposal of the NGLs. I would have hoped that some alternative could have been devised, but I note that Keith Joseph, George Younger and yourself regard their involvement as essential to achieve the objectives. I would not dissent, provided that the concerns about public expenditure and tax, expressed in my separate letter to Hamish Gray, can be met.

Finally, could I ask that your Department and the Department of Industry should keep Treasury and Inland Revenue officials much more closely in touch with their deliberations on this subject than has happened hitherto in view of the considerable tax and public expenditure interests involved; which Hamish Gray recognised in his letter to me of 9 December. In particular, I should like

Treasury and Revenue officials to be given the opportunity to comment on the guidance which you propose to give BNOC in support of the five objectives set out in the second paragraph of your minute to the Prime Minister.

I am sending a copy of this letter to our colleagues in E, Mr George Younger, Norman St John Stevas, Angus Maude and Sir Robert Armstrong.

*Yours sincerely*

*T. Mattes*

*for* JOHN BIFFEN

[Approved by the Chief Secretary  
and signed in his absence]



PRIME MINISTER

THE GAS GATHERING PIPELINE AND DISPOSAL OF NATURAL GAS LIQUIDS

1 I have seen David Howell's minute to you of 9 December and I am writing to lend my support to the approach he proposes.

2 From the petrochemical industry point of view I am entirely content that we should use BNOG and BGC as the wholesaler of a significant proportion of the natural gas liquids (NGLs). Although there are nuances of opinion amongst the various petrochemical companies - depending largely on whether they are part of an oil company - they are willing to deal with a wholesaler. ICI in particular sees advantage in this and is especially keen that BGC should be associated with BNOG in the disposal arrangements. The company has had satisfactory dealings with BGC in the past and respects its expertise in the handling of gaseous materials.

3 I welcome David Howell's intention to construct a system which ensures that the petrochemical industry gets this valuable feedstock on the most advantageous terms. I recognise that the interests of the Revenue might be thought to lead us to seek as high a price as possible. But I think this would be short-sighted. Our industrial interest lies very much in underpinning the petrochemical industry with a secure and competitive feedstock in the 1980s and 1990s, and we must not overlook the

/scope ...



scope for establishing a chain of downstream investments which will, along with the basic petrochemical industry, become an important incremental generator of tax revenue. It would, therefore, be premature in my view to set the maximisation of tax revenue from the basic raw material as an overriding criterion, particularly as revenue will not begin to accrue until 1984 at the earliest.

4 I welcome also the proposal to allow all potential suitors for the feedstock to bid for what they need. There is much dispute about the figures and it would be impossible - and invidious - for the Government to seek to allocate shares to particular companies. It is quite possible that the commercial negotiations will - together with the advice we give to the wholesalers - lead to a satisfactory outcome without further intervention from us.

5 I would have liked the statement to refer to our intention that the petrochemical industry should obtain the feedstock on the most advantageous terms and that British companies should get as many as possible of the orders for the goods and services associated with building and running the system. I recognise, however, the difficulties of balance in the statement. Provided we are agreed amongst ourselves about these points, I do not wish to press for changes to give them effect in the statement itself.

/6 ...

CONFIDENTIAL



3

6 I am sending copies of this minute to Members of E Committee, to George Younger, Norman St John Stevas, Angus Maude and Sir Robert Armstrong.

*Catherine Bell*  
pp K J

(approved by the Secretary of State and signed in his absence)

15 December 1980

Department of Industry  
Ashdown House  
123 Victoria Street

CONFIDENTIAL

*Ed. Mr Ingham*

PRIME MINISTER

*Mr Howell wishes to make the statement at Flag A - we think on the whole that a written answer will do. The Treasury have suggested one innocuous amendment - because they are concerned to avoid any loss of revenue through subsidised ethane prices (Flag B). Sir Keith is generally content (Flag C), and so is George Younger.*

THE GAS GATHERING PIPELINE AND DISPOSAL OF NATURAL GAS LIQUIDS

As you know I established last June an Organising Group to develop proposals for a new North Sea Gas Gathering Pipeline System. The Group has just reported to me on the handling of the natural gas liquids (NGLs) which will be extracted from the natural gas at St Fergus. The Group has:-

- Yes no* *Agree to* *with answer* *Wednesday, as* *announced* *by* *Treasury?*
- DL*
- i stressed that decisions on the routing of the NGLs are urgent to the overall time-table of the System;
  - ii invited me to decide how the NGLs, particularly the ethane (which will be produced by some 40 different licensees), should be aggregated into quantities sufficient for bulk contracts to be entered into for petro-chemical feedstock;
  - iii recommended that the ethane should be separated from the rest of the NGLs at St Fergus and piped separately to users with the processing of the remaining liquids to be carried out at Nigg Bay.
- 15/12*

I have been considering these recommendations with Keith Joseph and George Younger. Our objectives are:

- i to safeguard the operational efficiency and viability of the gas gathering system as a whole;
- ii to make as much ethane as possible available to the British Chemical Industry at the most advantageous terms;
- iii to safeguard our tax revenues and so reduce the PSBR;
- iv to protect licensees and other chemical companies against the monopolistic positions held by Shell/Esso and Dow;
- v to ensure that these companies do not use those positions to extract unreasonable charges from the licensees for the use of their processing facilities or land.



The Organising Group's recommendations on the pattern of disposal would suit us well and they, together with Shell, Esso, BP and ICI, have called upon HMG to declare its preference for disposal of NGLs in advance of commercial negotiations. Nevertheless, we are convinced that such overt action would risk the three latter objectives I mention above. (The first two objectives are, of course, protected by the substantial presence of BGC in the pipeline utility). Overt action could also attract opposition on the grounds of discrimination from the US Government and EEC, as well as from disappointed companies and Scottish regions. We are therefore convinced that commercial negotiations must precede any final decisions on the physical disposal pattern.

However, a decision on whether to develop Nigg Bay will be needed early in the New Year if delay to the Gas Gathering System as a whole is to be avoided. Commercial negotiations with the 40 or so different licensees producing the NGLs would not proceed fast enough.

BNOC has a crucial role to play in dealing with these two problems, by exercising its participation rights to buy a majority of NGLs and so, together with BGC, taking the lead as a wholesaler. Allowing BNOC to do this will not only accelerate the commercial negotiations but, since I shall be giving them guidance in support of the five objectives in my second paragraph, will also achieve the disposal pattern we want without overt intervention.

I do not propose that BNOC will have rights over the NGLs remaining to licensees after participation: some may wish to join in with the Corporation but others will not. Direct deals between licensees and ultimate users in respect of the remaining NGLs will act as a check upon BNOC.

I have discussed these proposals with Keith Joseph and George Younger and, despite our natural hesitation about using BNOC in this way, we are convinced that this is essential to achieve our objectives. Accordingly, I propose next week to announce that I wish commercial negotiations to proceed quickly and that, to facilitate this, HMG will not place obstacles in the path

CONFIDENTIAL



-3-

of the exercise by BNOG of its participation rights. I attach the draft text of the statement I propose to make. I would be grateful for your agreement to my proceeding in this way.

I am sending copies of this minute to our colleagues in E, to George Younger, Norman St. John Stevas, Angus Maude and Sir Robert Armstrong.

A handwritten signature in dark ink, appearing to be 'D.A.R.H.', written over a horizontal line.

(D.A.R.H.)

pp. Secretary of State for Energy  
(Approved by the Secretary of  
State and signed in his absence)

9 December 1980.



## DRAFT PUBLIC STATEMENT

Valuable natural gas liquids will be brought ashore by the new Gas Gathering Pipeline. The ethane, in particular, will be an important new feedstock for petrochemical plants in the UK. Timely completion of the facilities for handling these natural gas liquids is essential to the gas gathering system as a whole.

The Organising Group I set up in June has just made recommendations to me on the handling of these liquids. Their advice is that the ethane should be separated from the rest of the natural gas liquids at St Fergus and piped separately to users, with the processing of the remaining liquids to be carried out at Nigg Bay. They recommend that preparatory work should be carried out on an ethane line from St Fergus to Mossmorran, Grangemouth with an extension to Teesside and that an ethane line from St Fergus to Nigg Bay should also be considered. The Organising Group has stressed the urgent need for decisions on the routing of the NGLs. They have invited me to decide how the natural gas liquids should be aggregated into quantities sufficient for bulk contracts to be entered into for petrochemical feedstock.

I have invited the Organising Group to plan on the lines recommended while commercial negotiations proceed to determine the pattern of disposal of the NGLs.

At least seven companies have expressed an interest in purchasing the ethane as feedstock for ethylene manufacture and several licensees have expressed a need for reassurance that they will be able to regain access to natural gas liquids after onshore fractionation into component products. It is important that commercial negotiations for the sale and processing of NGLs should proceed quickly to a point which enables the pattern of onshore disposal to be settled. To facilitate this, clarity is needed on the rights and role of the various parties with an interest in the system. I have therefore today confirmed to the British National Oil Corporation that I shall not stand in the way of the exercise by the

/Corporation

Corporation of the rights to natural gas liquids which it enjoys under participation agreements. This will identify to prospective purchasers a substantial seller able to enter promptly into disposal commitments. The British Gas Corporation has informed me that it will cooperate with BNOG in this process, as appropriate. Taken together with the Organising Group's work on the terms for access to land or facilities needed for processing the rest of the NGLs, this should enable the pattern of the onshore facilities to be determined. There will be no obligation on licensees to sell the remainder of their natural gas liquid stream through the agency of BNOG.

X || I have invited the Corporation and the Organising Group to seek, in these negotiations to maximise petrochemical activity in the UK based on ethane. I have asked them to ensure, so far as possible, that facilities to process and use the NGLs will be available in accordance with the timetable envisaged for the gas gathering pipeline as a whole, including provision, if appropriate, for Norwegian liquids as they become available. They are to ensure that, subject to participation, licensees can recover their own material after fractionation and that later licensees and customers have access to the system on reasonable terms. I have made it clear that BNOG should not commit itself to investment in petrochemical plant.

I expect all parties to the commercial negotiations to conduct them constructively and speedily. It would not be acceptable for any one party to block agreement on reasonable terms if this threatened to impede timely completion of the Gas Gathering system.

X The Treasury has proposed the following amendment of this sentence -

4 I have invited the Corporation and the organising group to seek in these negotiations to maximise the national economic benefit and as part of this to recognise the importance of petro-chemical activity in the UK based on ethane."

MR LANKESTER

Gas gathering pipeline

Energy

I had a word with Energy about this since it refers to a "statement" next week. They say that Mr. Howell has not yet made up his mind what he wants to do, but that the choice is between a Written Answer and an Oral Statement next Wednesday. They want it to be on a separate day from the 7th Round Answers.

MAF  
disagrees

My view is that an Oral Statement would not be justified, and in any case there is an important Fish statement next Wednesday.

They will be coming back to us later with detailed handling proposals.

MS

9 December, 1980.



10 DOWNING STREET

THE PRIME MINISTER

8 December, 1980.

Dear Eldon,

Thank you for your letter of 30 October and its attached paper on the gas gathering line.

I agree with you on the importance of this project and the need to avoid delay.

In your note you suggest that the gas gathering line is being delayed because private finance will not be provided until there are firm gas purchase contracts in place, and that this will not happen until BGC offer producers a higher price for their gas in the light of world prices. I do not believe that this is so, and I hope that what I say below will reassure you that good progress is in fact being made.

It is understandable that the oil companies should press for higher gas prices and they have indeed been lobbying for this in different parts of the world. But their case is far from substantiated. The viability of the gas gathering line is based on known reserves of gas already explored. The full position is made clear in the BGC/Mobil report. You suggest that the oil companies are arguing for world parity pricing for gas (although some argue further for oil-parity pricing which is demonstrably against the interests of consumer nations). There is in fact no world gas market despite the claims of the oil companies because gas (unlike oil) is not so readily switched between markets, and where it is (in relatively small quantities, as for liquefied natural gas) the netback to the producer can be far lower than BGC is offering for

/gas for

gas for the pipeline. Indeed, even on the basis of comparing gas sales to fixed destinations, such as the Canadian/Mexican sales to the USA, BGC's current price offers are pretty comparable.

BGC have never expected that gas purchase contracts, which are complex documents, could be tied up for all or even most of the fields to be connected to the pipeline (many of which have not even got development approval) before substantial finance for the pipeline is needed. But I can assure you that, far from not meeting costs, the producers of gas from the central and northern sectors of the North Sea stand to make substantial profits.

The absence of gas throughput contracts is not delaying progress on the line. A recent Interim Report from the Organising Group showed that, in advance of the pipeline company being set up, momentum is being maintained through a joint venture agreed and financed between BGC, Mobil and BP. On the offshore work BP, who are in the lead there, are well into the pre-engineering phase, and expect the conceptual design largely to be completed by early next year. Work on preparation of tenders, on survey and on permit acquisition would then get under way. As for the onshore work, BGC have let a conceptual design study contract for the St. Fergus terminal and have work well advanced on the other onshore facilities. Land has been purchased and important planning permissions obtained. Overall, the Organising Group consider that a completion date of 1984/5 is still achievable, and they are working to that end.

As far as the purchase of Norwegian Statfjord gas is concerned, the Norwegian timetable has long been set on the basis that a final decision will be taken next spring. In the meantime, the Norwegians are understandably doing their best to promote a competitive market for their gas, and have gone to great lengths to promote competition between BGC, and other foreign purchasers, as well as considering plans to land the gas in Norway. With their General Election coming up next year, there is a good deal of politics as well as economics in the Norwegian position. Nevertheless, BGC have made what the Norwegians themselves acknowledge as a sensible offer, and if it is turned down it will not be for want of trying on our part. BGC, Department of Energy Ministers, and the

/Foreign Office

Foreign Office (including our Embassy in Oslo) have all paid detailed and continuous attention to the negotiations, with the aim of obtaining Statfjord gas for the new gas gathering line if at all possible. It would, of course, improve the economics of the gas line to obtain the Norwegian gas, but in its absence the line will still be a fully profitable venture as is made quite clear in the BGC/Mobil report.

On organisation and finance, I have already mentioned the current joint venture between the three partners that is carrying things forward for the time being. For the next stage, the Organising Group consider that an interim pipeline company should be formed until adequate gas throughput contracts are in place, and they are working on the structure and financing of that company. This company could be financed by equity, loans, and loan assurances from prospective users of the line and purchasers of gas and NGL. There now appear to be reasonable prospects, on banking advice, of raising funds for at least the first two or three years of construction ahead of the firm purchase/sales agreements which your information had suggested was a prerequisite of financing. As far as revision of the original cost estimates is concerned, we shall not be in a position to judge matters further until BP and BGC have produced new estimates based on the detailed engineering designs.

In summary, significant progress has been made to date and the picture is far more promising than you may have been led to believe. The Organising Group are well aware of the need for the project to be completed speedily and successfully and, given the experience and standing of the people and the organisations involved, I believe that we can be reasonably confident about the final outcome.

Yours ever,

(SGD) MT

Eldon Griffiths, Esq., MP.

## THE EXPLOITATION OF NORTH SEA NGL'S

Following the decision by Government to support the case for a Gas Gathering Network, various proposals are being put forward by petrochemical groups for the exploitation of the valuable natural gas liquids that will become available at St Fergus, after demethanisation of the associated gas.

### THE PROPOSALS

At Nigg on the Cromarty Firth, Highland Hydrocarbons Ltd, and Dow Chemicals have submitted proposals for gas fractionating and cracking plants (to produce ethylene) and the British Gas Corporation for a gas fractionating plant. All three proposals have received planning permission in principle from the Authorities concerned. The Highland Hydrocarbons proposal incorporates a three phase development, each phase consisting of a fractionating plant handling 1.5 million tons/per annum of raw NGL's and a cracking plant of 0.5 million tons/per annum capacity, using ethane ex the fractionater. Phase I would come on stream 1985/86 to coincide with the completion of the Gas Gathering Network and the associated de-methanisation facilities at St Fergus. Phase II would come on stream by 1988 or possibly earlier and Phase III in the early 1990's, the precise timing being dependent on NGL availability and market conditions at that time.

At Mossmorran on the Firth of Forth, Shell/Esso are to construct a fractionating and cracking facility to handle NGL's from their Brent Complex, East of the Shetlands. This project will fractionate about 2.0 million tons/per annum of NGL's initially and the cracker to be constructed by Esso, will have a capacity of 500,000 tons/per annum using ethane, ex the fractionater. The associated gas submarine pipeline connecting the Brent Complex with St Fergus has been completed and the demethanisation plant at St Fergus is under construction. Although delays have been experienced it is likely that the Mossmorran facilities will be on stream well before the completion of the Gas Gathering Network. Planning permission has been applied for for an NGL pipeline connecting St Fergus with Mossmorran and very recently, a modification was made to this application, whereby the diameter of this pipeline would be increased to 24" to permit a handling capacity of up to about 6.5 million tons/per annum of NGL's. Space is available on the Mossmorran site for further significant expansion of the fractionating and cracking functions and although no formal expansion plans have been announced, there is at least a possibility that further development will take place at Mossmorran, either later in the decade, or during the 1990's.

At Grangemouth on the Firth of Forth, BP are considering converting their existing crackers from naphtha to NGL's, either entirely, or in part. These crackers have been in operation for many years and their conversion would involve virtual rebuilding and considerable operational difficulties. However, there is no reason to suppose that this could not be done in time to meet the Gas Gathering Network deadline. Since naphtha is produced at the BP refinery at Grangemouth it is unlikely that it would be displaced entirely as the cracker feedstock. The quantity of replacement NGL's is therefore difficult to assess, but it should be at least 0.3 million tons/per annum, mostly ethane.

At Wilton on Tees-side, the recently completed ICI/BP cracker is capable of accepting NGL feedstock, although this and other plant at Wilton currently use naphtha, ex the refinery. ICI are also considering switching from naphtha/..

naphtha to NGL feedstock, but as in the Grangemouth case it is difficult to assess whether the switch will be total or partial. If total, the NGL requirement might amount to 0.8 million tons/per annum, mostly ethane. Conversion such as may be required could certainly be completed in time to meet the Gas Gathering Network deadline.

Grangemouth and Wilton are already connected by an ethylene pipeline and there is no doubt that the Shell/Esso NGL pipeline connecting St Fergus with Mossmorran could handle the NGL requirements of Mossmorran, Grangemouth and Wilton. A short connecting link would however be required between Mossmorran and Grangemouth, crossing the Firth of Forth.

At Grangemouth and possibly also at Wilton, additional NGL fractionating plant would be required, since the Shell/Esso pipeline is intended to handle raw NGL's.

#### NGL AVAILABILITY AND DISTRIBUTION

In considering NGL availability in the National context, it is appropriate to consider the total associated gas landings at St Fergus, ie. from the proposed Gas Gathering Network and from the Brent Complex. Estimates vary and uncertainties exist but in broad brush terms and taking the 15 year period 1986-2000 the NGL landing is likely to be of the order of 125 million tons or 5.0 million tons/per annum in the mid 1980's, rising to about 9.9 million tons/per annum in the mid 1990's, excluding any input from the Norwegian Sector. (Low Line).

Comparing the apparent requirements of Nigg, Mossmorran, Grangemouth and Wilton with the above estimates of NGL availability, the following situation should obtain:

<u>Low Line</u>	<u>Mid 1980's</u>	<u>Early 1990's</u>	<u>Mid 1990's</u>
Nigg	1.5 million t/a 34%	3.0 million t/a 46%	4.5 million t/a 47%
Mossmorran	2.0 " " )	2.0 " " )	3.3 " " )
Grangemouth	0.3 " " )66%	0.5 " " )54%	0.6 " " )53%
Wilton	<u>0.8</u> " " )	<u>1.0</u> " " )	<u>1.2</u> " " )
Total requirement	4.6 " "	6.5 " "	9.6 " "
Availability	<u>4.0</u>	<u>8.5</u>	<u>9.9</u>
Shortfall/surplus	(0.6) " (15%)	2.0 " 23%	0.3 " 3%
<u>High Line</u>	<u>Mid 1980's</u>	<u>Early 1990's</u>	<u>Mid 1990's</u>
Nigg	1.5 million t/a 33%	4.5 million t/a 47%	4.5 million t/a 47%
Mossmorran	2.0 " " )	3.3 " " )	3.3 " " )
Grangemouth	0.3 " " )67%	0.6 " " )53%	0.6 " " )53%
Wilton	<u>0.8</u> " " )	<u>1.2</u> " " )	<u>1.2</u> " " )
Total requirement	4.6 " "	9.6 " "	9.6 " "
Availability	<u>5.2</u>	<u>11.7</u>	<u>13.3</u>
Surplus	<u>0.6</u> " 11.5%	<u>2.1</u> " 18%	<u>3.7</u> " 28%



It will be seen that irrespective what happens at Nigg, Grangemouth and Wilton, Shell/Esso will proceed independently at Mossmorran and this involves an NGL flow South of at least 2.0 million tons/per annum initially and possibly increasing by at least 50% during the 1990's.

It is understood that BP/ICI claim that there is no case for a development at Nigg (contrary to the recommendations made in Energy Paper No. 44) and that, in consequence, all of the NGL's should be routed South.

The foregoing comparison of requirement and availability shows clearly that apart from a small shortfall initially, availability exceeds requirement, provided a fair and reasonable allocation is made.

If on the other hand, BP/ICI were to be allocated the entire NGL output of the Gas Gathering Network it would mean they would have to handle between 2.0 and 3.2 million tons/per annum initially, rising to between 6.5 and 8.3 million tons/per annum in the early 1990's and to between 6.6 and 10.0 million tons/per annum in the mid 1990's.

It will readily be seen that these quantities are far in excess of their estimated cracker requirements, even assuming total conversion from naphtha and allowing for further expansion. What then would BP/ICI propose to do with the large surplus, especially should the Norwegian NGL input materialise?

It should also be noted that neither BP nor ICI have any significant direct access to NGL's in their own right. The major owners of the NGL's are BNO, Mobil, Conoco, Texas Eastern, Total and Phillips, all of whom would presumably wish to have at least the freedom of choice as to the routing of their NGL's for processing and eventual disposal.

#### CRACKER OUTPUT PATTERNS

It is understood that suggestions are being made that as an alternative to directing all of the Gas Gathering Network NGL's South, all of the ethane from the BGC de-ethaniser at St Fergus should be allocated South, leaving the remaining propane butane and C5+ to be handled by the Nigg facility. Since ethane has by far the greatest value adding potential, Highland Hydrocarbons consider that this "compromise" would be even more grossly unreasonable and unacceptable.

A study of cracker output patterns comparing ethane, propane butane and naphtha as the feedstocks shows clearly that without access to ethane, it would not be possible to produce sufficient ethylene at Nigg to make a cracking operation commercially viable. This in turn would render "across the fence" manufacture of derivatives a non-starter. The Nigg operation would then be limited to liquids fractionating and shipping out with minimum value adding potential and nil inward investment in cracking facilities and "across the fence" developments.

The typical cracking patterns are as follows, using a 500,000 tons/per annum module (tons/per annum x 10<sup>3</sup>)

Feedstock Mode	100% Ethane		100% Propane		100% Butane		100% Naphtha	
Ethylene	400	80%	240	48%	210	42%	160	32%
Propylene	13	2.6%	78	16%	76	15%	75	15%
C4-C5+	17	3.4%	45	9%	103	21%	180	36%
Tail Gas	70	14%	137	27%	111	22%	85	17%
	<u>500</u>		<u>500</u>		<u>500</u>		<u>500</u>	

These patterns clearly show the necessity for an equitable allocation of ethane and Highland Hydrocarbons consider that whatever the NGL allocation, it should contain the proportion of ethane which occurs naturally and that no ethane should be bled off for any one destination at the expense of any other.

ETHANE SUPPLY/DEMAND

In general, the performance of the UK petrochemical industry in the past decade has compared somewhat unfavourably with that of Holland, West Germany, France and Italy.

Consequently, the UK groups are more than anxious to become less dependent upon naphtha as the principal petrochemical feedstock and to gain access to North Sea NGL's and especially to ethane as a replacement feedstock. As indicated above and unlike Shell/Esso, BP and ICI have relatively little NGL ownership in their own right. Their need to acquire sufficient NGL's to permit a switch (total or partial) from naphtha to NGL's is therefore fully understood and certainly accepted by Highland Hydrocarbons as being in the interests of the UK petrochemical industry and indeed the country. The only point at issue is the suggestion that BP and ICI should seek to acquire all, to the total exclusion of Nigg, since, whilst obviously in the interests of BP/ICI, would most certainly not be in the country's best interests.

Ethane being the most sought after feedstock it is worth again comparing cracker requirements with availability in terms of ethane, on the assumption that the average ethane content of the NGL's is likely to be about 39% by weight.

Low Line (Excluding Norwegian input)

	<u>Mid 1980's</u>	<u>Early 1990's</u>	<u>Mid 1990's</u>
Nigg	0.5 million t/a 26%	1.0 million t/a 38%	1.5 million t/a 39%
Mossmorran	0.5 " " )	0.5 " " )	1.0 " " )
Grangemouth	0.3 " " )74%	0.4 " " )62%	0.5 " " )61%
Wilton	<u>0.6</u> " " )	<u>0.7</u> " " )	<u>0.8</u> " " )
Total requirement	1.9	2.6	3.8
Availability	<u>1.6</u>	<u>3.3</u>	<u>3.9</u>
Shortfall/Surplus ( <u>0.3</u> )	(19%)	<u>0.7</u> 21%	<u>0.1</u> 3%

As in the case for NGL's, these figures indicate that sufficient ethane would be available to go round, provided it is shared on an equitable basis.

An interesting point arises in the event that all of the ethane from the Gas Gathering Network were to go South. This would mean ethane surplus to the Grangemouth/Wilton requirements, ranging from 0.2 million tons/per annum in the mid 1980's to 1.6 million tons/per annum in the mid 1990's, having to be disposed of other than to the crackers. This is difficult and expensive material to ship and if exported its value adding potential would be lost to the UK.

It is also understood that claims are being made that because there is excess UK cracking capacity for present market conditions any new cracking capacity could only be detrimental to the UK petrochemical industry. It is therefore further argued that in the UK context there is no case for a petrochemical development involving cracking at Nigg.

This line of reasoning is at least open to question, since market research undertaken by Highland Hydrocarbons shows quite clearly that most of the cracker output would be exported, either directly as ethylene or indirectly as ethylene derivatives from "across the fence" developments. Likewise most of the LPG's and C5+ from the fractionators would be shipped out to West European and US destinations with less than 15% likely to end up in UK refineries. Virtually the same can be said for the Mossmorran development, the main difference being that Shell/Esso are themselves the principal owners of the NGL's to be processed there. If therefore the new cracker argument is directed against Nigg for the reasons claimed, why is it not also directed against Mossmorran?

Yet another claim is being made that "cheap" ethane based ethylene production at Nigg would make it difficult for naphtha based ethylene ex Grangemouth and Wilton to compete and might result in the closure of naphtha based crackers, with resultant job losses in the South.

It has to be stated quite categorically that the price of ethylene or ethylene derivatives to be produced at Nigg would be dictated by market forces and not by any price differentials that might exist between naphtha and NGL's. Furthermore any price advantages that might be gained at Nigg would only be available via equity participation on the part of the buyers, or alternatively and indirectly from supply security via long term supply contracts.

Furthermore, since it is understood that BP and ICI appear to wish to switch from naphtha to NGL's, would not the ethylene produced at Grangemouth and Wilton be able to compete at least on equal terms with ethylene produced at Nigg and Mossmorran?

#### INWARD INVESTMENT

Firm interest is being expressed in the Highland Hydrocarbons proposals by two major West German petrochemical groups anxious to become less dependent on naphtha and attracted by the advantages of stability and supply security of the North Sea NGL's. These groups are interested not only in taking equity in the Nigg Cracker Project, but also in establishing "across the fence" facilities for the manufacture of ethylene and propylene derivatives, eg. HDPE, LDPE, ethylene glycol and polystyrene and possibly also MTBE derived from butane. The "across the fence" quantities presently indicated are of the order of 250,000 tons/per annum, or 65% of the output of the Phase I cracker, with the prospect of further significant expansion thereafter.

Other petrochemical groups in the EEC and elsewhere have approached Highland Hydrocarbons with similar interest in mind, but until such time as the Gas Gathering proposals are firmed up and more fully defined, Highland Hydrocarbons has decided to limit its involvement to Hoechst AG and URBKAG. These further approaches do, however, give a measure of the extent of interest in the potential export market for cracker production at Nigg.

Should the Nigg proposals develop in the three phases planned, it is now likely that there would be a distinct division between the fractionating and cracking functions, with a sharing of the common services such as power generation, jetties, pollution control, firefighting, reclamation, etc.

Approached on this basis, the capital expenditure for the fractionating function would amount to some £340 million and that for the cracking function, some £490 million at 1980 prices.

Considering only the cracking function, equity participation is likely to fall into three main categories:-

- Supplier Groups (owners of NGL's wishing to add value via the cracker) say 40%
- User Groups (users seeking a secure supply of petrochemical feedstock) say 30%
- Financial Groups (Institutions seeking to invest in North Sea NGL's) say 30%

The resulting equity profile for the cracker function therefore would be approximately as follows:

	<u>Phase I</u>	<u>Phase II</u>	<u>Phase III</u>	<u>Total</u>
Suppliers	96	52	48	196
Users	72	39	36	147
Financial	<u>72</u>	<u>39</u>	<u>36</u>	<u>147</u>
	<u>£240 million</u>	<u>£130 million</u>	<u>£120 million</u>	<u>£490 million</u>

It is of course difficult to say precisely at this stage how much of the equity might be true inward investment, but it is already clear that a majority of the potential suppliers and users would fall into the inward investment category (in particular US, West German and Japanese) and this might also apply to a lesser extent to the financial groups. Conservatively therefore, true inward investment in the cracker function is unlikely to be less than £250 million.

To this must be added the inward investment associated with "across the fence" developments at Nigg. On the basis of discussions held to date this might be of the order of £100 million initially, with further significant expansion associated with Phases II and III of the Nigg proposals.

It goes without saying that inward investment of this magnitude would have a very significant impact on the well-being of Scotland and of the Highland Area in particular. Therefore, irrespective of the arguments being put forward in favour of directing all of the NGL's South, it would appear that Government can scarcely afford to discount the benefits that would follow from a development at Nigg. In this connection, it must again be pointed out that if the NGL allocation to Nigg were to be significantly smaller than the proposed requirement of 1.5 million tons/per annum/phase, or should the ethane content of the allocation be severely curtailed, the cracking function would not be commercially viable and lacking a supply of ethylene, the West German interests would, without doubt, withdraw from further involvement and see to invest elsewhere.

#### ADDED VALUE

Of perhaps greater long term significance is the potential for adding value in the UK by cracking ethane to ethylene and possibly also propane to propylene at Nigg, as opposed to exporting the fractionated NGL's without further processing.

Since it is impossible accurately to forecast what market prices are likely to be in mid 1980's and beyond, value adding potential can only be examined with reference to current market prices.

On this basis and assuming no price escalation, the gross added value likely to arise from the cracking function at Nigg would be of the order of £90 million per annum in Phase I, rising to about £175 million/per annum in Phase II (allowing for some propylene production) and to about £255 million/per annum in Phase III.

Taking the period 1986-2000, the total gross value adding potential of the Nigg cracking function should therefore be in the range of £2,700 - £3,000 million at current prices.

To this should be added the value adding potential of "across the fence" manufacture of ethylene/propylene derivatives arising from an input of at least 250,000 tons/per annum.

#### PRICING

Looked at from the point of view of the suppliers of associated gas and irrespective of the actual price formula to be agreed for the raw gas, the methane content would probably account for at least 65% of the revenue accruing to the suppliers, calculated on a calorific value basis.

It will therefore be evident that until the methane (or specification gas) purchase price structure is settled, little progress is likely to be made. This is because the suppliers, that Government expects to take equity in the Gas Gathering System, must be assured that they will receive a reasonable return on their investments. Gas pricing is not a matter that can be left to free market forces to resolve, since the supply of gas to the National Grid is involved. It therefore follows that Government/or BGC, or both, should decide, as a matter of urgency, on the price to be offered to the suppliers so that a pricing formula can be negotiated.

It is also of importance to note that until this has been done, potential buyers of the raw NGL's are not in a position to negotiate an NGL price structure and consequently are unable to have meaningful discussions with potential buyers of the fractionated liquids.

The view currently held by Highland Hydrocarbons is that there are two "chicken and egg" situations that are frustrating meaningful development of Gas Gathering. The resolution of these situations depends essentially on Government being prepared to take decisions (a) on associated gas pricing and (b) on the distribution of NGL's, both of these decisions being largely political. Considerable urgency attaches to these decisions if the Gas Gathering deadline of 1985 is to be met and if the interest of potential "across the fence" investors is to be sustained.

#### JOB NUMBERS

It is understood that one of the arguments put forward in support of the allocation to the South of all of the Gas Gathering Network NGL's is that if this is not agreed crackers at Grangemouth and Wilton may have to be shut/..

shut down with the loss of between 200 and 300 jobs. However, as demonstrated under "Ethane Supply and Demand" above, equitable sharing should ensure that sufficient ethane would be available to satisfy the requirements of these particular crackers. It is therefore to be assumed that they would continue in operation after conversion and the implied job loss would not arise.

On the other hand, the Nigg development will create some 350 permanent jobs in Phase I, with a further 100 in "across the fence" manufacturing. In Phase III the permanent job total is expected to increase to about 750 with corresponding additional "across the fence" job creation. This does not include the indirect job creation connected with maintenance and other support services.

During construction up to 2,000 jobs would be created, spread over a period of between eight and ten years.

*cc Mr Whitson*

*A*



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

01 211 6402

*Ann Griffiths*

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Mr Howell has now submitted a revised draft <sup>(Part A)</sup> to Eldon Griffiths, and hopes that you will be prepared to sign this without a meeting.

David Whitson has discussed all this with Mr Howell and his officials and is impressed that they have got a grip of this project; it also seems that Eldon Griffiths is more interested in lobbying for the oil companies than in getting a good deal for industrial and domestic consumers.

2 December 1980

CONFIDENTIAL

Tim Lankester Esq  
Private Secretary  
10 Downing Street  
LONDON  
SW1

*Have signed because  
have had to  
revise.*

Dear Tim,

You mentioned on the telephone that the Prime Minister was not fully convinced by the draft reply to Eldon Griffiths', MP, letter of 30 October. A revised reply, approved by my Secretary of State is attached. Mr Griffiths does not question the composition of the Organising Group and approves of the guidelines my Secretary of State gave to the Group. It may nevertheless be helpful if I recall the considerations which Ministers had in mind when they approved the Secretary of State's proposals for the organisation of the gas gathering system.

The oil companies would have preferred full joint venture financing but this would have led to the pipeline being financed through tax reliefs to the detriment of the PSBR. Ministers therefore favoured the private utility pipeline company concept suggested by Mr Howell. They also agreed that it was desirable that BGC should have a significant stake (eventually agreed as 30% of the equity) in the company in order to ensure that the consumers' interests in keeping tariffs down were represented, to encourage the participation of the Norwegians, to keep up the momentum of the project and to influence the placing of orders for the construction of the line.

These arguments are just as valid today. If we were to change at this stage the structure of the Organising Group or of the proposed pipeline company, there would inevitably be delay. There would be no chance of achieving the 1984/85 completion date; we would as a consequence definitely lose Norwegian gas; and the price of gas to the consumer would rise through higher pipeline tariffs eventually. As it is, the oil companies realise that they have to bargain with BGC: that bargaining is proceeding; and the Organising Group is making useful progress and has recently advised Mr Howell that it still considers achievable the target completion date of 1984/85.

The oil companies would, of course, like the highest price they can get for the gas. But, if this were conceded, it would be at the expense of both the industrial and domestic consumer in the UK. We could recover through taxation some of the profits of the international oil and gas companies. The tax system is, however, inevitably somewhat leaky and some of the profits which should accrue to the Exchequer would find their way overseas. Having BGC as the customer means that we get the gas ashore on terms which are fair and reasonable to both parties. And we can in turn ensure that

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CONFIDENTIAL



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any excess profits of BGC are channelled to the Exchequer.

Mr Griffiths in his letter suggests that the pipeline is being delayed because of the inability to obtain private finance and that the stumbling block is BGC's unwillingness to offer prices acceptable to North Sea producers. This is not so. Progress is being maintained through temporary financing arrangements between BP/Mobil/BGC and there are reasonable prospects, on the latest bank advice, of financing the early years of construction ahead of such contracts. In the meantime BGC has started contractual negotiations with one of the significant suppliers of gas to the pipeline, and we understand that these negotiations are going well.

Some of the points in this letter would, as you will appreciate, not be appropriate to include in the reply to Mr Griffiths. But I thought this background would be helpful in considering that reply. If there is any further information you need, please let me know.

Yours ever,

*J D West*

J D WEST  
Private Secretary



CONFIDENTIAL

DRAFT LETTER FOR THE PRIME MINISTER TO SEND TO:-

TYPE M

Eldon Griffiths Esq MP  
House of Commons  
LONDON  
SW1A 0AA

12

GAS GATHERING LINE

Thank you for your letter of 30 October and its attached paper on the gas gathering line.

I agree with you on the importance of this project and the need to avoid delay.

In your note you suggest that the gas gathering line is being delayed because private finance will not be provided <sup>until</sup> ~~until~~ there are firm gas purchase contracts in place, and that this will not happen until BGC offer producers a higher price for their gas in the light of world prices. I do not believe that this is so, and I hope that what I say below will reassure you that good progress is in fact being made.

It is understandable that the oil companies should press for higher gas prices and they have indeed been lobbying for this in different parts of the world. But their case is far from substantiated. The viability of the gas gathering line is based on known reserves of gas already explored. The full position is made clear in the BGC/Mobil report. You suggest that the oil companies are arguing for world parity pricing for gas (although some argue further for oil-parity pricing which is demonstrably against the interests of consumer nations). There is in fact no world gas market despite the claims of the oil companies because gas (unlike oil) is not so readily switched between markets, and where it is (in relatively small quantities, as for liquefied natural gas) the netback to the producer can be far lower than BGC is offering for gas ~~for~~ the pipeline. Indeed, even on the basis of comparing gas sales to fixed destinations, such as the Canadian/Mexican sales to the USA, BGC's current price

/offers...

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offers are pretty comparable. ~~It is hard to see why a purchaser should deal other than in the particular market place for purchase of gas if it is to serve the interests of its consumers best. The alternative is inevitably higher gas prices than would otherwise be the case both for industry and for domestic consumers.~~ BGC have never expected that gas purchase contracts, which are complex documents, could be tied up for all or even most of the fields to be connected to the pipeline (many of which have not even got development approval) before substantial finance for the pipeline is needed, though currently they are in serious discussions on gas to become available for the line. <sup>but</sup> I can assure you that, far from not meeting costs, the producers of gas from the central and northern sectors of the North Sea stand to make substantial profits ~~for what in the absence of a gas gathering line would in many cases have been gas flared in the course of oil production. The new gas line will therefore be of great benefit to both producers and the nation.~~

*in admin of line* // The absence of gas throughput contracts is not delaying progress on the line. A recent Interim Report from the Organising Group showed that <sup>being set up</sup> ahead of the pipeline company momentum is being maintained through a joint venture agreed and financed between BGC, Mobil and BP. On the offshore work BP, who are in the lead there, are well into the pre-engineering phase, and expect the conceptual design largely to be completed by early next year. Work on preparation of tenders, on survey and on permit acquisition would then get under way. <sup>As for</sup> On the onshore work, BGC have let a conceptual design study contract for the St Fergus terminal and have work well advanced on the other onshore facilities. Land has been purchased and important planning permissions obtained. Overall, the Organising Group consider that a completion date of 1984/5 is still achievable, and they are working to that end.

As far as the purchase of Norwegian Statfjord gas is concerned, the Norwegian time-table has long been set <sup>on the basis of</sup> at a final decision <sup>will</sup> to be taken next Spring. <sup>later</sup> Meantime, the Norwegians are understandably doing their best to promote a competitive market for their gas, and have gone to great lengths to promote competition between BGC, ~~the~~ <sup>and</sup> ~~Continent,~~ and others, <sup>foreign purchasers,</sup> as well as considering plans to land the gas.

CONFIDENTIAL

3.

in Norway. <sup>at</sup> There is a good deal of politics as well as economics in the Norwegian position - with their General Election <sup>coming up</sup> next year, Nevertheless, BGC have made what the Norwegians themselves acknowledge as a sensible offer, and if it is turned down it will not be for want of trying on our part. BGC, Department of Energy Ministers, and the Foreign Office (including the <sup>on</sup> Embassy in Oslo) have all paid detailed and continuous attention to the negotiations, with the aim of obtaining Statfjord gas for the new gas gathering line if at all possible. It would, of course, improve the economics of the gas line to obtain the Norwegian gas, but in its absence the line will still be a fully profitable venture as is made quite clear in the BGC/Mobil report.

On organisation and finance, I have already mentioned the current joint venture between the three partners that is carrying things forward for the time being. For the next stage, the Organising Group consider that an interim pipeline company should be formed until adequate gas throughput contracts are in place, and they are working on the structure and financing of that company. This company could be financed by equity, loans, and loan assurances from prospective users of the line and purchasers of gas and NGL. There now appear to be reasonable prospects, on banking advice, of raising funds for at least the first two or three years of construction ahead of the firm purchase/sales agreements which your information had suggested was a prerequisite of financing. As far as revision of the original cost estimates is concerned, we shall not be in a position to judge matters further until BP and BGC have produced new estimates based on the detailed engineering designs.

In summary, significant progress has been made to date and the picture is far more promising than you may have been led to believe. The Organising Group are well aware of the need for the project to be completed speedily and successfully and, given the experience and standing of the people and the organisations involved, I believe that we can be <sup>reasonably</sup> confident about the final outcome. ~~provided that all concerned, including Government and the oil companies, lend their full support to making a success of the project to the time-table.~~

NORTH SEA GAS GATHERING

# A hard game for the referee

By Sue Cameron, Chemicals Correspondent

**M**R. DAVID HOWELL, that most fastidious of UK Energy Secretaries, is being dragged into joining the scrimmage in progress about gas from the planned new £1.1bn North Sea pipeline. The fact that Norway now seems certain to decide against pumping gas from her own huge Statfjord field into the new line, merely increases the pressures on Mr. Howell to make some decisions of his own.

Officially he is being asked to do no more than act as referee for the British National Oil Corporation, the British Gas Corporation, assorted major oil companies and a rowdy pack of chemical producers. (This is a game where any number can play.)

But unfortunately for Mr. Howell there are no set rules. Teams have scant respect for match officials and their tactics tend to include lawful "bribery" plus bullying—especially where the referee is concerned.

Play so far has certainly been divertingly dirty. A libel lawyer could live well for the rest of his days on some of the stories being put around by the various interested parties. But Mr. Howell cannot allow himself the luxury of regarding the North Sea gas gathering battle as a spectator sport.

A number of decisions have to be taken before the offshore pipeline and associated petrochemical projects can go ahead and those decisions can only be taken by Government. The main ones are:

- The role of the British National Oil Corporation—BNOC.
- The role of the British Gas Corporation.
- Which companies should be the first to receive natural gas liquids—NGLs—from the new offshore pipeline to use as raw materials in the making of petrochemicals.
- The limits—notably the lower limits—to be set on the price of all the gases.

Mr. Howell will not have to bear the burden of this decision-making entirely unaided. Advice will pour in from all quarters—not least from the official pipeline organising committee.

The committee, which includes representatives from British Gas, Mobil and British Petroleum, was set up in June when the Government gave agreement in principle to the construction of a North Sea gas gathering system. The Government announced that the new line would be built and operated by a pipeline company in which British Gas would have a 30 per cent stake. The task given to the organising committee was to decide how the rest of the pipeline company should be structured and financed.

But there are several difficulties facing the committee. One is that nobody knows exactly how much gas there will be. Statfjord—the Norwegian state oil company, Shell and the U.S.-based Mobil are now expected to say they want the gas they lift from the Statfjord field to go to Norway and to Germany. This decision—ratified by the Norwegian parliament—would substantially reduce the amount

of gas available for the new UK gas gathering system.

The new line will gather various different types of gas—methane, ethane, propane and butane—from a number of North Sea fields. Methane is the gas used in the home for cooking and heating and as an industrial fuel. It will all go to the nationalised British Gas, which has a monopoly over it.

The new line will also enable large amounts of oil to be extracted. Associated gases come with the oil and these could either be gathered—by the new line—or flared. But the



IT now looks likely that the UK energy and chemical industries will have to live without gas supplies from Norway's portion of the big Statfjord Field in the North Sea. But there will be enough gas from UK fields to make the £1.1bn pipeline network worthwhile and to give chemical companies something to fight over, and Mr. David Howell, the UK Energy Secretary (above) plenty to think about.

UK Government would not permit the gases to be flared and therefore one of the most important justifications for the new line is that it will enable the UK's oil production to be boosted.

Oil and methane are the primary reasons for constructing the new gas gathering system. But it will also carry other gases—each one suitable for use as a petrochemical feedstock.

The point about these other gases is that two thirds of them could go to BNOC which is also a state-owned energy company. BNOC's equity interest in the North Sea will automatically give it a gross 12 per cent of the ethane, propane, butane and other NGLs coming through the new offshore line.

But the Government may allow BNOC to exercise its option under state participation agreements to buy a further 51 per cent of the NGLs—or what is left of them once the Government has taken its own 12.5 per cent royalty share. Mr. Howell could also allow BNOC to handle the Government's royalty share on its behalf.

BNOC would almost certainly welcome the chance to take the lion's share of the gains. It has

already said it is interested in setting up an NGL trading arm and it has even talked about entering the field of petrochemicals production. There would be a number of advantages to giving BNOC a leading role:

- The corporation would clearly have an extremely powerful say on NGL pricing. It could be argued that this would be much quicker and more efficient than the alternative of leaving a number of petrochemical companies to negotiate prices with the equally large number of oil companies which will actually be producing the gases in the North Sea.
- The Government could exercise permanent sway over the whole gas gathering operation by virtue of the fact that it has almost unlimited powers over what BNOC does.

The next team to come up for inspection by Mr. Howell is the British Gas Corporation. British Gas will clearly have a major part to play in the whole operation because of its monopoly over methane. But unconfirmed reports suggest the corporation would like to exercise a neat monopoly over the other gases as well—a prospect that makes the hard-playing lads in the chemical teams pale with horror.

The next team to come up for inspection by Mr. Howell is the British Gas Corporation. British Gas will clearly have a major part to play in the whole operation because of its monopoly over methane. But unconfirmed reports suggest the corporation would like to exercise a neat monopoly over the other gases as well—a prospect that makes the hard-playing lads in the chemical teams pale with horror.

What is more likely is that British Gas will act as carrier for the NGLs once they have been landed at St. Fergus on the Scottish coast. The corporation has already said it would like to build a de-ethanising plant at St. Fergus and ethane gas is the NGL most of the chemical companies would prefer to use as feedstock. It would therefore be logical for British Gas to build and run the land lines taking ethane from St. Fergus to petrochemical sites.

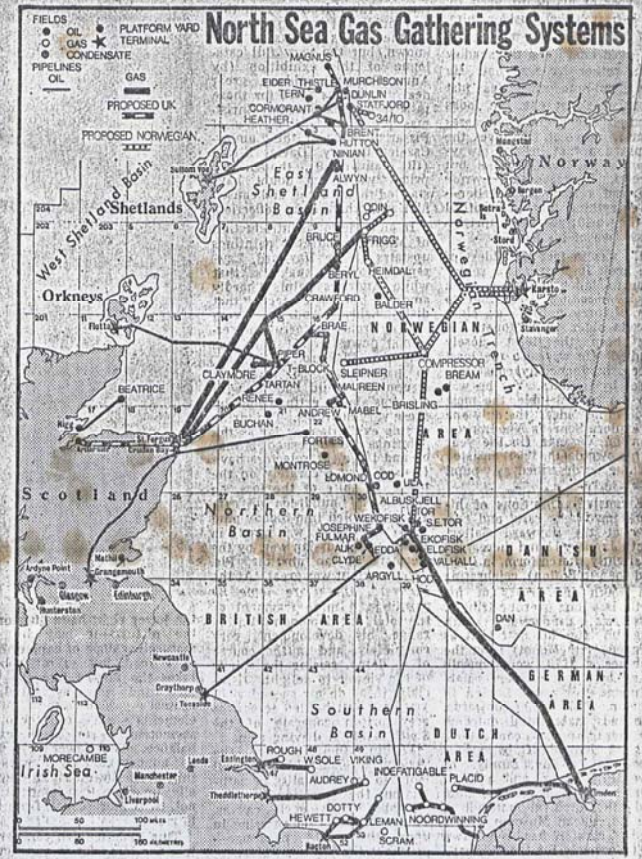
The corporation has peculiar powers under the Gas Act when it comes to the construction of land lines. It does not have to obtain planning consents—the most time consuming aspect of building a land line—and it does have compulsory purchase rights.

But it will probably be up to Mr. Howell to decide whether the provisions of the Gas Act should apply to these NGLs in the same way they apply to methane.

It is believed British Gas has put forward a plan to the main pipeline organising committee suggesting that it be allowed to build a land line south from St. Fergus to the existing petrochemical plants owned by the "gang of four."

The gang of four—Shell Chemicals UK, Esso Chemical, Imperial Chemical Industries and Bp Chemicals—wants all the ethane likely to be available in the next 10 years to go to its existing plants at Grange-mouth (BP) in Scotland and Wilton (ICI and BP) on Teesside and to a new chemicals complex being built at Moss-morran (Shell/Esso) in Fife.

The chances are that Mr. Howell regards the gang of four and its petrochemical rivals for North Sea NGLs with some distaste. He is, after all, gently spoken old Etonian with a



slightly different air and fine white hands. The chemicals fraternity is altogether earlier. More souls have been committed to their section of the pitch than anywhere else. Their leading players—apart from the gang of four—are the U.S.-based Dow Chemical, the U.S.-based Occidental and the UK-based Highland Hydrocarbons.

Dow, Highland and Occidental are offering a number of inducements to Mr. Howell. They include:

- Dow's offer of £400m worth of petrochemical investment in the UK at Nigg Bay on the Cromarty Firth in Scotland plus an eventual bonus of 15,000 new jobs in the area.
- Highland's bumper package of £800m worth of new investment in petrochemicals plus plans for the gang of four to have the ethane it wants.
- Occidental's promise of a £200m chemicals development at Peterhead near St. Fergus with the possibility of new process technology that could produce low cost, high quality linear low density polyethylene plastic.

In contrast, the members of the gang of four believe in strong arm methods. They are privately confident that they carry enough political clout between them to win the day. Unconfirmed reports suggest that this confidence will be fully justified. In the meantime they are making thinly veiled threats to shut some of their own existing plants.

Their best card is that they could build a land line—with the help of British Gas perhaps—and modify their present plants to use ethane as feedstock before anyone else would be ready to use it. The weaknesses in their case are that their maximum investment would be only some £150m and that some of their plants would be almost obsolete by the time they were converted to take gas as a raw material.

The gang of four only trooped belatedly onto the field after the half-time whistle had blown. Apparently they failed to realise that the match was on—which must raise some questions about their commercial prowess. But they have now set to with a will and demanded that Mr. Howell

makes a decision by Christmas on whether or not there should be a pipeline from St. Fergus to the south.

Even without Norwegian Statfjord NGLs, the latest estimates suggest there will be around 5m tonnes of gas liquids available each year by 1995-96. This figure could rise as new discoveries are made and estimates of North Sea recoverable reserves are revised.

But Mr. Howell will still have to decide the order of allocation. For the chemical buyers of NGLs will need to have their plants ready—whether newly built or modified—by the time the gases start flowing through the offshore line. Speedy decisions are also required on the parts BNOC and British Gas are to play. It is though that each month's delay will add tens of millions of pounds to the final cost of the North Sea gas pipeline.

Back in the dressing-room, some of the chemical players are already becoming impatient. They are suggesting that perhaps the Prime Minister should be brought on as an extra referee with a more powerful whistle.

1. MR. SANDERS <sup>MS</sup>
2. PRIME MINISTER

Gas Gathering Pipeline

If you want to change the general thrust of the reply to Eldon Griffiths, I think you will need a meeting with Mr. Howell. The draft reflects the decision that was taken in E in June (Flag A) and Mr. Howell's announcement (Flag B)

Ian MacGregor of course raised this issue with you. If you wanted a meeting, I could get a note on his ideas via David Young, and Sir Keith could be invited to expound on them.

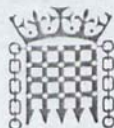
Yes  
Please  
ms

I should perhaps point out that one of Eldon's main criticisms is that BGC are not prepared to offer the gas producers high enough prices. But one of the reasons for giving BGC a 25 - 30% stake was to ensure that consumer interests were protected and tariffs kept down. Similarly, it was felt important to keep BGC in the picture because otherwise the existing chemical companies would gain control of all the gas and keep out potential new entrants such as Dow and others in the future.

Your point - that we could have cheap gas for our own chemical industry if the pipeline was owned by a consortium of users who would be charged transfer prices - would only arise if the chemical companies are also the equity owners of the gas. In fact, this is not the case except in a minority of cases. When the gas producers are not also chemical producers, they will ask for the best price they can get.

It might still be the case that the pipeline would be completed more quickly without BGC. But the Department of Energy deny this emphatically: they argue, on the contrary, that to remove BGC now would hold up completion and put at risk our access to the Norwegian gas. Finally, there is not much of a public expenditure issue here. BGC's equity stake will cost £50 - 80m over the next 5 years; and there should be a good return on it.

TL



HOUSE OF COMMONS  
LONDON SW1A 0AA

2nd December, 1980.

North Sea Gas-line

Further to my letter sent to the Prime Minister about the North Sea gas-line, I attach a disturbing article from the Sunday Times. This bears out the sad news my sources gave me, namely that Britain is losing, if we have not already lost, the Norwegian gas in the Statfjord field.

Is it not now inevitable that the economics of gasline will be made less attractive?

I am copying this letter and enclosure to the Prime Minister so that she may take Mr. Offerdal's article into account when replying to my original letter.

(Dictated by Mr. Griffiths and signed in his absence)

The Rt. Hon. David Howell, M.P.  
Secretary of State,  
Department of Energy,  
Thames House South,  
Millbank,  
S.W.1.

c.c. Rt. Hon. Margaret Thatcher, M.P.

# Norway snuffs out UK gas plan

by Harald Offerdal

BRITAIN'S planned pipeline for gathering North Sea gas received a major setback last week. The Norwegian state oil company, Statoil, has presented an alternative plan for landing the gas from its section of the Statfjord field in Norway rather than sending it to Britain through the British gas gathering pipeline. This plan is almost certain to be approved by the Norwegian parliament early next year.

Without the Norwegian gas, which would have accounted for 30% of the throughput, the profitability of the British project will be seriously undermined. It will also be a major blow for British Gas which had hoped to use the Norwegian gas

to meet projected demand from industrial users.

Statoil's plan is to build a 190-mile pipeline from Statfjord to Korsto north of Stavanger, where the gas will be processed and factories erected. This will create 700 new jobs and the Norwegian trade unions naturally support this proposal. From Kosto a new pipeline will be built to a terminal platform 100 miles west of Stavanger and then a farther 100 miles onto the Ekofisk field where it will be linked to the existing pipeline to Emden in Germany.

The attraction of the new plan is that the Heimdal field, which is estimated to contain

35,000 million cubic metres of gas, can be linked to the system through a 100-mile long pipeline to the terminal platform west of Stavanger. This alone will increase the total amount of gas reserves in the system from the 70,000 million cubic metres, which the Statfjord field is estimated to contain, to over 100,000 million cubic metres. In addition a number of other Norwegian fields can be linked to the system in the future.

The Ekofisk pipeline to Emden in Germany already operates with a surplus capacity which is expected to increase to 15,000 million cubic metres a year by 1990. The pipeline from

Statfjord to Norway will be designed to carry 8,000 million cubic metres a year.

Norwegian oilmen are wondering what will happen to the British share of the Statfjord, about 16%, when the Norwegian Statfjord gas is landed in Norway. During an official visit to Norway one month ago the British minister of state for oil and energy, Hamish Gray, said that the British share was not for sale and would be landed in Britain whatever Norway decided to do.

The Norwegians have taken an increasingly sceptical view of the British alternative because they fear the pipeline will simply not be completed in time, that is by January 1986.

I have a lot of sympathy  
with Nelson's letter. That's why I  
have not signed the reply. If the  
pipeline were run wholly by a consortium  
of users - surely we could have steps  
taken for our own benefit willingly - because  
only beneficiaries would be involved. not,

CONFIDENTIAL



10 DOWNING STREET

THE PRIME MINISTER

Thank you for your letter of 30 October and attached paper on the gas gathering line. I entirely agree that we should pay close attention to progress on this important project.

The current position is as follows. On the physical aspects, the momentum is being kept up: BP, who are in the lead on the offshore work, are well into the pre-engineering phase, and expect the conceptual design largely to be completed by early next year. Work on preparation of tenders, on survey and on permit acquisition would then get under way. On the onshore work, BGC have let a conceptual design study contract for the St. Fergus terminal and have work well advanced on the other onshore facilities. In a very recent report to the Secretary of State for Energy, the Gas Gathering Organising Group (BP, Mobil, British Gas) consider that a completion date of 1984/85 is still achievable, and they are working to that end.

On organisation and finance, the Organising Group consider that an interim pipeline company should be formed to carry the project forward until adequate gas throughput contracts are in place, and they are deliberating about the structure and financing of that company. This company could be financed by equity, loans, and loan assurances from prospective users of the line and purchasers of gas and NGL.

/ The Norwegians

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The Norwegians will decide next Spring on the destination of Norwegian Statfjord gas. There is no clear indication of whether or not they will accept BGC's offer. If they turn it down, it will certainly not be due to procrastination on our part; BGC, the Department of Energy and the Foreign Office (including the Embassy in Oslo) have all paid detailed and continuous attention to the negotiations, with the aim of obtaining Statfjord gas for the new gas gathering line if at all possible. However, Norwegian domestic politics as well as economics will be heavily involved and the final outcome is difficult to forecast at this stage.

You mention the suggestion that BGC's prices for new Northern Basin supplies are causing or likely to cause delay. BGC have never expected that gas purchase contracts, which are extremely complex documents, could be tied up for all or even most of the fields to be connected to the pipeline (many of which have not even got development approval) before substantial finance for the pipeline is needed. I can assure you that, far from not meeting costs, the producers of gas from the central and northern sectors of the North Sea stand to make substantial profits for what in the absence of a gas gathering line would in many cases have been gas flared. The new gas line will therefore be of great benefit to both producers and the nation.

I also know of no reason at this stage to expect the project to cost more than the original estimates which were, of course, cast in terms of 1980 money. We shall not, however, finally be in a position to judge matters until BP and BGC have produced new estimates based on the detailed engineering designs.

In summary, you will see that significant progress has been made and that the picture is not as unpromising as you may have been led to believe. There are naturally interplays of interests in a project of this importance with many bodies involved; and

/ no-one

CONFIDENTIAL

- 3 -

no-one can be sure at this early stage how things will turn out. Nevertheless, the Organising Group are well aware of the need for the project to be completed speedily and successfully and, given the experience of the people and the organisations involved, I believe that we can be confident about the final outcome.

Eldon Griffiths, Esq., M.P.

CONFIDENTIAL



SECRETARY OF STATE FOR ENERGY

THAMES HOUSE SOUTH  
MILLBANK LONDON SW1P 4QJ

01 211 6402

Nick Sanders Esq  
Private Secretary  
10 Downing Street  
LONDON  
SW1

17 November 1980

Dear Nick,

GAS GATHERING PIPELINE: LETTER OF 30 OCTOBER FROM ELDON GRIFFITHS

I attach a draft reply for the Prime Minister to send to Eldon Griffiths. The draft sets out the current position on the project. As it says, significant progress has been made, and the picture is not as unpromising as Mr Griffiths may have been led to believe. The Secretary of State has only very recently received an Interim Report on progress from the Organising Group, and he intends to meet the Group at an early date in order to probe matters further.

Yours ever,

J D West

J D WEST  
Private Secretary



DRAFT LETTER FOR THE PRIME MINISTER TO SEND TO:

Eldon Griffiths Esq MP  
House of Commons  
London SW1A 0AA

62

for MP

(CONFIDENTIAL)

cc IG 10/11

ms

GAS GATHERING PIPELINE

Thank you for your letter of 30 October and attached paper on the gas gathering line. I entirely agree that we should pay close attention to progress on this important project.

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On organisation and finance, the Organising Group consider that an interim pipeline company should be formed to carry the project forward until adequate gas throughput contracts are in place, and they are deliberating about the structure and financing of that company. This company could be financed by equity, loans, and loan assurances from prospective users of the line and purchasers of gas and NGL.



The Norwegians will decide next Spring on the destination of Norwegian Statfjord gas. There is no clear indication of whether or not they will accept BGC's offer. If they turn it down, it will certainly not be due to procrastination on our part; BGC, the Department of Energy and the Foreign Office (including the Embassy in Oslo) have all paid detailed and continuous attention to the negotiations, with the aim of obtaining Statfjord gas for the new gas gathering line if at all possible. However, Norwegian domestic politics as well as economics will be heavily involved and the final outcome is difficult to forecast at this stage.

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I also know of no reason at this stage to expect the project to cost more than the original estimates which were, of course, cast in terms of 1980 money. We shall not, however, finally be in a position to judge matters until BP and BGC have produced new estimates based on the detailed engineering designs.



In summary, you will see that significant progress has been made and that the picture is not as unpromising as you may have been led to believe. There are naturally interplays of interests in a project of this importance with many bodies involved; and no-one can be sure at this early stage how things will turn out. Nevertheless, the Organising Group are well aware of the need for the project to be completed speedily and successfully and, given the experience of the people and the organisations involved, I believe that we can be ~~entirely~~ confident about the final outcome.

COMMONWEALTH OF INDEPENDENT STATES  
LONDON

file BK

Th. E. GRIFFITHS

North Sea Gas

4 November 1980

Overdue

Chasepl MS

17/11

I wrote to you yesterday enclosing a copy of a letter the Prime Minister had received from Eldon Griffiths, M.P. about North Sea gas. The Prime Minister has now seen Mr. Griffiths' letter, and has commented that she has great sympathy with his views.

I should be grateful if those drafting the reply could take this into account.

N J SANDERS

Julian West, Esq.,  
Department of Energy

KLB

DSS

File

3 November 1980

I attach a copy of a letter the Prime Minister has received from Eldon Griffiths MP.

I should be grateful if you could suggest a draft reply for the Prime Minister to send to Mr. Griffiths, to reach us here by Friday 14 November.

N. J. SANDERS

Julian West, Esq.,  
Department of Energy.

BK



File

DSC

3 November 1980

I am writing on behalf of the Prime Minister to thank you for your letter of 30 October about North Sea gas pricing. I will place it before the Prime Minister and you will be sent a reply as soon as possible.

**N. J. SANDERS**

**Eldon Griffiths, Esq., M.P.**

BK



2

10 DOWNING STREET

PRIME MINISTER

This letter from Eldon Griffiths is about North Sea gas pricing and the new gas gathering pipeline.

We will let you have a draft reply.

*As soon as possible. I have great sympathy with view. Mrs K.G. not.*

3 November 1980

FROM: Eldon Griffiths, M.P.

ccTG  
8/11



HOUSE OF COMMONS  
LONDON SW1A 0AA

Dear Margaret

30th October, 1980.

The North Sea stands out like a light in our surrounding gloom - but one aspect of its development is a cause for deep concern. The high hopes for early completion of the big new gas line seem likely to founder on the Gas Council's monopoly. This is being used in a manner that suits the immediate commercial interests of British Gas, but could endanger the early supply of gas (and chemical feed-stock) to British industry. We should be open to political attack from both the Opposition and industry if this project is not completed before the end of this Parliament.

I have set out the reasons for my anxiety on the attached paper which, of course, I have taken up with David David Howell and Hamish Gray. However, in view of the vital importance of this project to the country and our Party's fortunes at the next election, I am sure you will wish to see it personally.

Rt. Hon. Margaret Thatcher, M.P.

### North Sea Gas Pricing

1. Prospects of an early start on the new large diameter gas pipeline to collect gas in the central and northern sectors are receding. The 1984/85 target date for landing the first gas in Britain, as forecast in the House, almost certainly will not be achieved.

2. Despite long and careful discussion no firm decisions have been reached on how the gas line is to be financed. The volumes of gas it will carry (which clearly affect its overall feasibility) are also in doubt because the Norwegian sector gas may now be piped elsewhere - largely due to U.K. procrastination.

3. The main cause of the delay is the inability to obtain private finance. The Government guidelines are sound, despite reservations the producers are prepared to go along with them. But private finance has not been forthcoming because:

- a) Private lenders require guarantees from British Gas and/or equity owners of production before they will put up the cash.
- b) The equity owners of production cannot undertake these commitments until they have firm purchase/sales agreements with British Gas.

4. The stumbling block is that British Gas is still unwilling or unable to offer prices acceptable to North Sea producers. Its most recent proposals go some way towards bridging the gap; but no large producer sees any prospect of meeting the costs of finding and developing large scale sources of gas in the Central and Northern sectors on the basis of the Gas Council's offer.

5. The producers view their U.K. gas reserves as having a value equivalent to the market value in similar North West European markets. To them it seems a contradiction for BNOG to be purchasing oil from producers at world parity prices, while British Gas offers significantly less than the equivalent of world prices for gas.

6. As a monopoly British Gas is in a position to say "take it or leave it". But unless they are assured of more realistic prices the producers say they cannot afford to come to terms; and in this their banks support them.

Continued.



HOUSE OF COMMONS  
LONDON SW1A 0AA

7. Failure to resolve this problem gives rise to two serious consequences:

- a) The entire gas line project is now going to cost much more. Its minimum cost is bound greatly to exceed the government endorsed estimates of March 1980.
- b) While the U.K. has delayed Continental customers have opened negotiations with the Norwegians for the purchase of gas from their adjacent Statfjord field. Should this Norwegian gas be lost to the U.K. financing of the gas line will become more difficult, and less gas will be landed in Britain. British industry will have less abundant sources of gas-based feed stock.

8. Conclusion

Until agreement is reached between British Gas and the producers (and the banks), progress on this new gas line is unlikely to be achieved under the Government's guidelines. British Gas, for commercial reasons that no doubt appear correct to its Board, is making use of its statutory monopoly to resist offering a price that reflects the greater risks and higher costs of further exploration and development. For wider national reasons, the Gas Council should be pressed to reach agreement with the oil producers quickly. If this is not done, this pipeline will not be built until the later 1980's, and no gas from this source will be landed in Britain during the lifetime of this Parliament.



cc Eng

R/2/10

*Energy*

*Top copy on  
from PDI Sept 80  
Correspondence with  
Dr Armand Hammer.*

10 DOWNING STREET

THE PRIME MINISTER

3 October 1980

Dear Dr Hammer

Thank you for your letter of 6 September on the timescale for construction of the gas gathering pipeline. I am most grateful for your offer of a discussion with the Occidental pipeline team under Mr. Daniel, and would like to have the benefit of the advice you have offered, As you probably know, David Howell has invited B.G.C., B.P. and Mobil to form an Organising Group for the pipeline. Their responsibilities include the technical work concerned. The Organising Group are best placed to benefit from discussion with your pipeline experts, and David Howell will arrange for their Chairman, Sir Denis Rooke, to contact Mr. Daniel direct.

(sgd) M T

Dr. Armand Hammer.

jfh

Original, Eln Bl,  
Sept 80, Correspondence  
from Dr Armand Hammer

ca Mr Filder



Energy

10 DOWNING STREET

THE PRIME MINISTER

3 October 1980

Dear Dr. Hammer,

Thank you for your letter of 26 September.

Gordon Reece is leaving his post in the Conservative Party and I am delighted to learn that he is joining such an excellent company as Occidental. It is most kind of you to offer to make his services available to us if we have any need for him on specific assignments in the future. I shall certainly be in touch with you if this arises.

We shall miss Gordon. He is full of infectious enthusiasm for his work. I am sure you will be very happy with his services.

All good wishes.

Dr. Armand Hammer.

Yours sincerely  
Margaret Thatcher

Original; ECU 1st  
 Sept 80, Correspondence  
 from Dr Armand  
 Hammer



10 DOWNING STREET

THE PRIME MINISTER

3 October 1980

Dear Dr. Hammer,

Thank you for your letter of 6 September about the oil taxation 'ring fence' provisions, following our discussion on the trip to Flotta.

I would certainly like to encourage successful North Sea oil companies to plough their oil production profits back into the UK economy. Your proposal, that investment in new energy related projects should be allowed immediate tax relief against oil production profits inside the 'ring fence', is an interesting approach. As you recognise in your letter, my main difficulty lies in the revenue losses which would arise. In framing tax reliefs of the kind you suggest, it would be very difficult to restrict them only to additional investment proposals. Almost inevitably more generous immediate relief would have to be given to all new energy related investment - including a great deal which would have gone ahead without the need for tax concessions. On any reckoning, investment in new UK energy related work in the next few years is likely to be very substantial even without new incentives: indeed, you have yourself announced prospective investment of some \$1½ billion by a single company. Your proposal is one which I and my Treasury colleagues will certainly bear in mind as we look at arrangements in this field in the future. I am most grateful to you for writing to me to set it out.

I cannot thank you enough for the confidence and faith you are putting in Britain's future. It is now some weeks since my visit to Flotta, but the memory will stay with me for many years to come. Yours sincerely  
 Margaret Thatcher

Dr. Armand Hammer.



Original Ecom B/L,  
Sept 80, Correspondence  
from Dr Arnold Hammer  
10 DOWNING STREET



THE PRIME MINISTER

2 October 1980

Dear Dr Hammer

Thank you for your letters of 6 September about your proposals for petrochemical development at Peterhead and the refinery project at Canvey Island. I welcome proposals which will add value in the United Kingdom to our North Sea oil resources.

As I understand the position, you are no longer thinking in terms of a conventional refinery at Canvey Island. Instead you propose to produce from fuel oil lighter products likely to be in greater demand over the coming years. We share your views about the likely development of the oil products market. I am sure you are right to explain your change of plans fully to the local interests in Canvey Island so as to avoid misconceived opposition. I hope your staff will keep the relevant Departments here fully informed.

I am writing to you separately about our gas gathering pipeline. From that letter, you will see that David Howell has invited British Gas, B.P. and Mobil to form an organising group for the pipeline project. This is responsible also for advising on the suitability of proposed facilities onshore for taking the natural gas liquids as they become available. Your staff may wish to keep in touch with the Group on the Peterhead project. The Group, and the subsequent pipeline company, will not however own the N.G.L.s transmitted through the new line; and cannot, therefore, sell them. I note that you are in contact with B.N.C.C. about the possible purchase of its gas liquids carried through the new line.

/ Other companies have

278

Other companies have also offered to purchase for petrochemical use the liquids from the new line. However, your proposal to use the ethylene from the suggested cracker for polymerisation into linear low density polyethylene is interesting. Obviously the further downstream a petrochemical venture goes the greater the added value and the more employment it generates. Your particular proposals will therefore receive close consideration from all those involved in the supply of feedstock.

signed

MT

Dr. Armand Hammer



SECRETARY OF STATE FOR ENERGY  
THAMES HOUSE SOUTH  
MILLBANK LONDON SW1P 4QJ  
TELEPHONE: 01-211 3000  
01 211 6402

2 pgs.

Top copy on  
Even Post Sept 1980  
Correspondence with  
Dr Armand Hammer

Mike Pattison Esq  
Private Secretary  
10 Downing Street  
Whitehall  
LONDON  
SW1

29 September 1980

Dear Mike,

Thank you for your letters of 8 and 12 September about the correspondence from Dr Hammer of Occidental. This reply deals with points raised on the gas gathering project.

I attach a note on the main constraints, as currently seen, which affect the time-table for the project. The main point to note is that our fears of delay relate mainly to the onshore work (the pipeline terminal and facilities for handling natural gas liquids) rather than to offshore pipelaying. However, the possibility of delays is a threat to every part of such a complex project, and we would certainly recommend that the Prime Minister take up the offer of advice in Dr Hammer's 6 September letter. I attach a draft reply to that letter; the draft suggests that Occidental's advice would be of most benefit to the gas gathering Organising Group (BGC, BP and Mobil) whose tasks include advancing the technical and operational basis for the project.

You also asked about BSC's capability to supply the special steels needed for the project. BSC is well aware of the major opportunity which the project provides, and has been engaged in a major exercise, involving investment at Hartlepool and Redcar, to get itself into a position of being able to meet the probable steel requirements of the project. At this stage, the exact material specifications and delivery schedules for the project have not been finally established. However, BSC is continuing to liaise closely with BGC and BP on the technical details. In all of this activity BSC is being strongly supported by the Department's Offshore Supplies Office.

In the final analysis, however, price and delivery dates will be important determinants, and there will be strong competition from abroad, particularly from Japan and West Germany. Against this background BSC has much to do since over the years it has been singularly unsuccessful in supplying the oil companies' needs for offshore line-pipe. However, significantly, this year it has won 2 contracts of this nature (BGC's Morecambe Bay project and - still confidential - for BP's West Sole gas field) and these will provide it with the opportunity to establish credibility for further orders. It is vital therefore that BSC perform well on these contracts and the Offshore Supplies Office is monitoring the position closely. BGC



(2)

itself, with our encouragement, is deliberately promoting a closer relationship than in the past with BSC in order to keep them informed as early as possible on future pipeline requirements so that BSC is placed in a favoured position to compete.

I shall be writing to you separately about the Occidental letters you sent me on 9 September, dealing with the proposed polyethylene plant and with Canvey Island.

*Yours sincerely,*

*Geoff Dart*

G S DART  
Private Secretary

DRAFT LETTER



Armand Hammer Esq  
Chairman and Chief Executive Officer  
Occidental Petroleum Corporation  
10889 Wilshire Boulevard  
Suite 1500  
Los Angeles  
California 90024  
USA

GAS GATHERING PIPELINE

Thank you for your letter of 6 September on the timescale for construction of the gas gathering pipeline. I am most grateful for your offer of a discussion with the Occidental pipeline team under Mr Daniel.

David Howell tells me that the area currently thought most likely to be critical to the timing of the gas gathering line is the construction of the related onshore facilities rather than the laying of the pipeline itself. However we would not wish for a moment to relax on the time-table for the pipelaying given the overall complexity of the project and the scope for delay.

I would therefore like the project to have the benefit of the advice you have offered. As you probably know, David Howell has invited BGC, BP and Mobil to form an Organising Group for the pipeline project, and their responsibilities include the technical work concerned. The Organising Group are best placed to benefit from discussion with your pipeline experts, and David Howell will arrange for their Chairman, Sir Denis Rooke, to contact Mr Daniel direct.

PRIME MINISTER



## GAS GATHERING PIPELINE

### MAJOR POINTS ON TIME-TABLE

#### (i) Offshore

BP, as offshore operator for the project, will not have completed a detailed construction programme before the end of the year. In the interim they accept that 1984/5 completion is likely to be attainable. The present outline envisages tendering for pipeline manufacture beginning January 1981 and award of contract in April 1981. Following finalisation of the specifications, in the light of detailed design engineering, manufacture would begin. Deliveries of pipe-lengths to coating yards would begin in April 1982, so that the bulk of the line could be laid offshore during summer 1983. Trenching and tie-in of the pipe to individual fields would occupy 1984, with hydrostatic testing, drying-out and commissioning beginning towards the end of 1984 and rendering the line fully operational in 1984/5.

#### (ii) Onshore

2. Construction and commissioning of the terminal and natural gas liquids (NGL) facilities would be expected to take at least  $3\frac{1}{2}$  years. Site preparation must therefore be complete by (at the latest) early 1982, which necessitates start of site work in mid-1981 (earlier for any NGL facilities at Nigg, as the land has first to be reclaimed). Before site preparation can begin, planning permission must be obtained, the site must be acquired, the construction contract put out to tender and awarded, and sufficient design work done to provide a basis for the construction contract and site preparation.

3. However, this time-table, which is already tight, is subject to a number of uncertainties particularly in relation to the NGL facilities:

- (i) it is not yet clear what the NGL disposal route will be. (There is interest in Nigg, Mossmorran/Grangemouth/Teesside, and now from Occidental in Peterhead.);
- (ii) there is a cautious optimism on the prospects for obtaining planning permission, though in the light of the delays experienced on the Mossmorran project there could be difficulties resulting in delay;



(iii) in some cases there may be problems in site acquisition, particularly for a development at Nigg by someone other than Dow (Dow control the suitable land).

4. As regards the St Fergus terminal, BGC have acquired the land and have already applied for planning permission. There remains the risk of construction delays: the time-table for Shell/Esso's terminal under construction at St Fergus is suffering considerable slippage.

(iii) Conclusion

5. The critical item in the project time-table at present is completion of onshore facilities to handle specification gas and the natural gas liquids (NGLs).

Gas Division  
18 September 1980

Original, Leon Bl, File  
Correspondence from  
Dr Armand Hammer  
of Occidental on American  
investment in the UK.



Gregg

ds.

10 DOWNING STREET

From the Private Secretary

8 September 1980

Dear Julian

BF 12.9.80  
BF 30.9.80

We told you by telephone on Friday of the announcement made by Occidental Petroleum of decisions in principle for further investment in the UK. The announcement was made by Dr. Armand Hammer whilst he was escorting the Prime Minister on her visit to Flotta. It covered reactivation of the company's Canvey Island project, on a basis which would be voluntarily acceptable to the local population; an ethylene plant at Peterhead, probably costing \$500 million; and a semi-submersible floating platform for work on relatively smaller North Sea fields.

As was made clear in Occidental's presentation to the Prime Minister and in Dr. Hammer's later conversations with her, the timing of his remarks was in part geared to support Occidental's applications under the seventh licensing round. Dr. Hammer also handed the Prime Minister the attached letter on the subject.

Mrs. Thatcher was much impressed with what she saw at Flotta - both in terms of rapid and efficient execution of the project, smooth operation, and excellent relations with the local authority and local people from the outset. She will want to reply in terms which are as forthcoming as possible to the attached letter, and it would be most helpful if you could let me have a draft by Friday 12 September.

In the course of the Prime Minister's conversations at Occidental, she followed with particular interest the discussion of the laying of the company's pipelines. She commented that she was told that four years would be needed to lay the UK gas gathering pipeline, and that she was very keen to hear suggestions as to how this timescale might be reduced. It would be most helpful if you could let me have a note on the main constraints of the timetable. The Prime Minister has also particularly asked whether the special steels which will be required for the pipeline are likely to be obtained through BSC.

I should be grateful if you could let me have a note on these points as soon as possible.

Yours ever

Mike Pattison

Julian West, Esq.,  
Department of Energy.

ds.



OCCIDENTAL PETROLEUM CORPORATION

10889 WILSHIRE BOULEVARD · SUITE 1500

LOS ANGELES, CALIFORNIA 90024

(213) 879-1700 · (213) 477-0066

Top copy on  
Enron file Sept 80  
Correspondence with  
Dr Armand Hammer

ARMAND HAMMER  
CHAIRMAN AND  
CHIEF EXECUTIVE OFFICER

6th September, 1980.

The Rt. Hon. Margaret Thatcher, M.P.  
Prime Minister and First Lord of the Treasury,  
10 Downing Street,  
London, SW1.

Dear Prime Minister,

I have been giving a lot of thought to your expressed desire to find a way, if possible, to shorten the time, which you say was estimated at four years, for building the gas gathering pipeline.


Without being immodest, I am frank to say that our people believe that we have laid our gas pipeline in the shortest time, and in the most efficient way of any pipeline operator in the North Sea.

Unfortunately, when you were shown around Flotta and asked the question, our pipeline team headed by our Senior Vice President - North Sea, Leon Daniel, was not present - most of the people are in Aberdeen or on the platforms, and Mr. Daniel himself was in London. I had a conference in London with Mr. Daniel, and I am convinced that he could be of great help to you and the Government in an advisory capacity. He has many suggestions for shortening the estimated time of four years, which we would if this were our project, and if our operations were dependent on our stopping flaring and getting our gas beneficially to market. If you think well of my suggestion, Mr. Daniel would be pleased to meet with Mr. David Howell and/or Mr. Hamish Gray, to go over the planning which has already been done, and to make any suggestions which might be of value to the Government.

Fortunately, our entire team is intact and while we are not in a position to undertake this work because of our commitments, we would be happy, if we could be of service in an advisory capacity. This offer is made without any view to compensation.

Mr. Daniel's telephone number is (0224) 574588, and in his absence Miss. Kate Graham, his secretary, will know where to contact him.

Sincerely yours,



Armand Hammer.

Energy

JK to see MAP 24/6.

B

01 211 6402

The Rt Hon Sir Geoffrey Howe MP  
 Treasury Chambers  
 Parliament St  
 London  
 SW1

19th June 1980

*See Section*

GAS GATHERING PIPELINE: CHAIRMAN OF THE ORGANISING COMMITTEES

Thank you for your letter of yesterday, agreeing to the appointment of Dennis Rooke as chairman of the Organising Committee and so allowing us to maintain the momentum of this important and profitable project. However, your letter did make me wonder whether you were not under some misapprehension about my attitude to BGC on this and indeed other issues.

So far as the pipeline is concerned, the basic point is that, as with any transmission system, a necessary condition for raising the finance is a firm commitment from a customer to buy what is to be transmitted. In this case, BGC is the sole gas utility and so must inevitably carry the bulk of this commitment. Therefore, BGC's equity share has nothing to do with Rooke's success as a negotiator. It is merely best business practice that it should have a slice of the equity and of the project's benefits strong enough to counter pressure from the gas producers whose interests will be in seeing gas prices and the pipeline tariff rise as fast as possible. (There is plenty of evidence in current international developments of how we could expect the producers to behave if left to their own devices).

You mention other issues between ourselves and BGC on which we "might have" asked for something in exchange for giving Rooke the chair of the Organising Committee, referring in particular to Wytch Farm. However, I believe that my own disposals scheme, described in E(DL)(80)6 which is, I understand, to be taken next Tuesday, is a more sensible approach than forcing a quick sale of Wytch Farm to a single buyer and will yield greater proceeds. There are numerous other issues between

us and BGC - their monopsony, pricing strategy, pay etc - on each of which we shall of course require either Rooke's co-operation or his compliance. I'm sure you will accept that I should pursue these, in the light of Ministers collective decisions, in the way I judge best.

I am copying this letter to the recipients of yours.

*Wm*

D A R Howelll

*Dave*



Prime Minister

To see, in view of your recent contacts with Sir D. Rooke.

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

18 June 1980

MP 18/VI

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

*David Howell*

GAS GATHERING PIPELINE :  
CHAIRMAN OF THE ORGANISING COMMITTEE

Thank you for your letter of 13 June about the chairman of the Organising Committee of the gas gathering pipeline.

My office have now told yours that following our discussion about the chairmanship I accept the appointment of Sir Denis Rooke. I do so with some reluctance, since I feel it is a pity that there is no suitable private sector man to chair a committee to organise what is essentially a private sector venture. I do, however, take it - and I know you agree with this - that there is no question of appointing Sir Denis Rooke or any other public sector man to chair the Pipeline company when it is set up. I would see great difficulty in that, since this is supposed to be a private sector venture.

But even given that Sir Denis Rooke is to be appointed, I think we might, as I suggested to you, have tried to obtain some advantage from his appointment. He is, for example, causing problems for our policy on disposals; and we might have extracted from him, as part of a deal involving his appointment to chair the organising committee, his co-operation in the sale of BGC's share in Wytch Farm so that the proceeds count towards this year's asset disposal total of £0.5bn. Or we might have used the carrot of his appointment to try to reduce BGC's equity stake in the company to nearer 25 per cent. In short, I think that the best way of dealing with Sir Denis Rooke, who is above all a tough negotiator, is for us to negotiate toughly with him.

I am sending a copy of this letter to the Prime Minister, the Secretary of State for Industry and to Sir Robert Armstrong.

*We had a word about this yesterday*

*Yours*

GEOFFREY HOWE

*Geoffrey Howe*

Prime Minister  
Energy



DEPARTMENT OF INDUSTRY  
ASHDOWN HOUSE  
123 VICTORIA STREET  
LONDON SW1E 6RB

TELEPHONE DIRECT LINE 01-212 7691  
SWITCHBOARD 01-212 7676

From the  
Minister of State  
Lord Trenchard

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

R 19/6

18 June 1980

Dear David

GAS GATHERING PIPELINE

Keith Joseph has asked me to reply to your letter of 16 June.

I am content with the terms of the announcement you propose to make on Thursday 19 June.

I am sending copies of this letter to all members of E Committee and to Sir Robert Armstrong.

*Yours  
Tom*

LORD TRENCHARD



Energy

Mick - To see  
MS  
Dunn  
2 P

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

Mr Howell to  
announce next  
steps on the  
gas gathering pipeline  
on Thursday.  
16th June 1980

The Rt Hon Sir Keith Joseph Bt MP  
Secretary of State for  
Industry  
Ashdown House  
123 Victoria Street  
London  
SW1 6RB

PL  
4/1

De Kirk

mt

GAS GATHERING

Following our discussion on Wednesday, 11th June, I shall be announcing the next steps on gas gathering by means of the attached answer to a written PQ. I understand officials of your Departments have been consulted on the broad outlines of the text.

I propose to make the announcement on Thursday, 19th June. I shall, however, as a diplomatic courtesy, be sending the text 24 hours in advance in confidence to Mr Gjerde in Norway via our Ambassador.

I am sending copies of this letter and attachment to my other colleagues in E.

Yours ever

D A R Howell

DAR



DRAFT PQ AND A TO ANNOUNCE NEXT STEPS ON GAS GATHERING

Q: To ask the Secretary of State what plans the Government has for a gas gathering system in the northern North Sea?

A: At today's high energy prices, and with growing industrial demand for natural gas, our offshore gas reserves represent an increasingly precious national resource. The Government is determined to make the most of that asset and to eliminate uneconomic waste of gas by flaring. I particularly welcome therefore the report from the study team from the British Gas Corporation and Mobil, which is published today as Energy Paper No. 44. Copies have been placed in the Libraries of both Houses.

The report recommends that a new offshore gas pipeline system should be built consisting of a 36" diameter trunk line from the Statfjord area via Quadrant 16 to St. Fergus, with a northern spur from Magnus and a larger southern spur from Fulmar. Fields along the route would be connected by lateral lines, and provision made to link in later fields. The system would be designed to take a high proportion of natural gas liquids, to minimise offshore processing costs.

At a terminal at St. Fergus gas to British Gas specifications would be separated from the natural gas liquids. The report has concentrated on piping those liquids for fractionation at Nigg Bay, but also considers other possibilities. The total cost of the project is estimated at about £1.1 billion.

The Government has given careful consideration to the study team's report and the implications for the nation of the general recommendations. Applications for pipeline authorisations and planning permissions will need to be made in due course. We consider, however, that a pipeline system along the general lines recommended would be in the national interest. The integrated gas gathering concept would, through its economies of scale, both allow the development of smaller gas accumulations and facilitate the most economic collection of larger gas deposits. It should also



reduce wasteful offshore flaring, and encourage further exploration within its catchment area. On land, it should help maintain supplies of gas and an integrated approach to disposal of the liquids should provide valuable opportunities for petrochemical development. Once flows have built up the pipeline would each year land gas and liquids worth some £1½ billion.

Various schemes have been proposed for the possible use of the gas liquids and these will require careful consideration. Where there are alternatives it will be necessary to evaluate the advantages and disadvantages in terms of maximising the value obtained by the nation from the natural gas liquids and of strengthening the UK's position in petrochemicals.

The Government considers it important that a gas gathering system should be constructed as quickly as possible, with the aim of bringing gas ashore from 1984/5. I have therefore invited British Gas, Mobil and BP to form, together with a financial adviser, an Organising Group. This will develop proposals for how a pipeline organisation could best be structured and financed as a private utility transmission company outside the public sector. I would envisage British Gas taking up [30%] of the equity of such a company, with the remainder of the equity being offered in appropriate proportions to financial institutions, licensees and customers for the NGL and, if Norwegian gas should be committed for transmission through the system, Norwegian concerns. I also envisage that the company would be financed substantially by loan finance raised from the markets, and without Government guarantee. The Organising Group intends to progress its work so that a pipeline company can be formed in the late autumn.

The detailed design of the facilities will require active assistance from the licensees of the fields from which the gas will be transmitted. I hope that all those licensees will give every assistance to the project.





Energy

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PRIME MINISTER

Gas Gathering Line  
(E(80) 52)

BACKGROUND

The British Gas Corporation (BGC) and Mobil have recommended that a gas gathering pipeline should be built as soon as possible to link the fields in the northern basin of the North Sea to St. Fergus in North East Scotland. Their report is not a formal pipeline application. But the Secretary of State for Energy recommends that he should make an early announcement that the Government is in favour of the construction of the line; that it endorses the setting up of a private sector company, in which BGC would have a stake, to build and operate it; and that it agrees with the early formation of an Organising Group consisting of BGC, Mobil, BP and a financial adviser to work out the detailed proposals.

2. He has discussed these proposals with the Chief Secretary who is content with them in general but may, I understand, wish to propose a lower shareholding for BGC than the 35 per cent envisaged by the Secretary of State.

3. The capital cost is in the range of £0.8 billion to £1.3 billion, depending on the final extent of the system and the onshore facilities. It is generally agreed that the economic case is robust and that the scheme compares well with the alternative of collecting gas through existing pipelines and flaring other gas or leaving it in the ground. It is thought that the pipeline would also stimulate the development of further oil and gas reserves. The recommendations are judged to be technically sound.

4. It is also agreed that the aim should be to complete the pipeline by 1984-85. This would avoid further wasteful flaring. It would be useful in convincing the Norwegians that they should pipe gas from their fields to us through the new line rather than attempt to construct another line to their own western coast. In this connection you will have seen the telegram of 27th May from the Ambassador to Norway.



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5. The pipeline would be constructed and operated by a private sector company. To balance the interests of consumers and of the private sector operators, the Secretary of State for Energy is thinking in terms of a 35 per cent share for BGC; 35 per cent for financial institutions; 20 per cent for producers; and 10 per cent for other consumer interests including the Norwegians. The Government would not generally be involved in determining the tariffs, though the Secretary of State could intervene on appeal to him and, if necessary, the Monopolies and Mergers Commission could be asked to investigate.

6. If the debt/equity ratio were 80:20 as proposed, BGC's contribution to the equity would be in the order of £50 to £80 million over the next five years. Provided that BGC did not control the company, the rest of the financing costs would not score against the Public Sector Borrowing Requirement (PSBR).

7. The pipeline would also land natural gas liquids (NGLs) used for petrochemical purposes. One possibility is to pipe these westwards to a greenfield site at Nigg Bay. Another, which BP would prefer, would be to pipe it south to facilities in Scotland and the North of England. This will be considered further by Departments and by the proposed Organising Group.

HANDLING

8. After the Secretary of State for Energy has introduced the paper you might ask the Chief Secretary to comment on the implications for the PSBR. The Foreign Secretary may wish to comment on the reactions of the Norwegians. Lord Trenchard can speak on the interests of the chemical industry who would use the NGLs, and on the procurement possibilities for British manufacturing industry. The Secretary of State for Scotland may also have points to make.

9. The main questions are:-

(a) Should the Government endorse the general proposal?

There seems to be a strong economic case for encouraging the project to go ahead as soon as possible. If this is accepted the discussion can focus on questions about the role of the Government and of BGC.



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(b) What should be BGC's shareholding?

The case for giving BGC a minority holding is that they can then influence the development of the pipeline and the decisions on the tariffs for transmission. Their presence may also be necessary to win the participation of the Norwegians. But the Committee will wish to consider whether their stake needs to be as high as 35 per cent. 25 per cent would be sufficient to give them a blocking vote on changes in the Articles of Association which will incorporate the ground rules for the tariff system.

(c) Are the PSBR costs acceptable?

£50 million to £80 million over five years is relatively small in the context of the total borrowing of the nationalised industries. But BGC's contribution would be higher if the proportion of equity to debt were to be increased. It is also essential that the arrangements should not be modified in a way which would give BGC effective control of the company, since it would then have to be classified to the public sector and the whole of its financing would score against PSBR. The proposed Organising Group will be making detailed recommendations about the financial arrangements, including the debt/equity ratio. It will be important to make clear to them the limitations of BGC's role, and Ministers will wish to consider their detailed proposals when they are available.

(d) Who should run the Organising Group?

The paper is silent on the important question of who should chair the Organising Group. If BGC's role is to be confined, that points against Sir Denis Rooke. You might ask the Secretary of State for Energy to consult further with you and the Chancellor on this question.

(e) What are the procurement implications for British Industry?

This project should give very significant opportunities for orders from the British Steel Corporation and from other British manufacturers. The possibilities for the Government influencing the placing of these

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orders will be limited by the fact that the company will be a private sector one and naturally concerned with how competitive are the tenders offered. But subject to that, and to avoiding European Community charges of giving overt preference to British companies, the Committee will wish to ask the Secretary of State for Energy to take all steps possible to ensure that a high proportion of the orders go to British manufacturers.

CONCLUSIONS

10. Subject to the discussion you will wish to record conclusions:-
- (a) Endorsing the general proposal to construct the pipeline under a ✓ private sector company, with the shareholding spread between consumer, producer and financial interests.
  - (b) Agreeing the stake that the British Gas Corporation should have in ✓ this company.
  - (c) Endorsing the proposal for an Organising Group to work out the ✓ detailed proposals, but
  - (d) Inviting the Secretary of State for Energy to clear with you and the Chancellor who should chair this Organising Group and to report in due course when it has made its recommendations.
  - (e) Inviting the Secretary of State for Energy to ensure that, so far as possible, a significant proportion of the production contracts go to British manufacturing industry.
  - (f) Approving an early announcement of the decisions on (a) and (e).

(Robert Armstrong)

10th June 1980

File

Energy

DSG

9 June 1980

Thank you for your letter of 6 June.  
The Prime Minister has seen and noted  
Oslo telegram no. 104 of 27 May, which  
you enclosed with your letter.

M. A. PATTISON

Denis Walker, Esq.,  
Department of Energy.

5.



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

Prime Minister  
E will be taking a  
report on the pipeline  
next week.

M A Pattison Esq  
Private Secretary to the  
Prime Minister  
10 Downing Street  
London  
SW1

*ms*

*MA 6/VI*

6 June 1980

*Dear Mike*

As I mentioned to you over the phone, I am attaching a copy of a telegram from HM Ambassador to Norway of 27 May concerning Statoil's proposal to land Norwegian Statfjord gas in Western Norway and describing three actions which he considers would materially assist BGC's effort to buy that gas.

My Secretary of State feels the Prime Minister may find this telegram interesting.

*Yours ever,*

*Denis*

Denis Walker

GPS 900

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CONFIDENTIAL

FM OSLO 271250Z MAY 80

TO ROUTINE FCO

TELEGRAM NUMBER 104 OF 27 MAY 80

INFO ROUTINE DEPT OF ENERGY (FOR PHILIP JONES, HERZIG AND SPAIN)  
INFO ROUTINE DEPT OF INDUSTRY (FOR BINNING, SAUNDERS IBB AND SUMNER  
CT4) AND INFO ROUTINE SCOTTISH ECONOMIC PLANNING DEPT (FOR MCCRONE)

NORWEGIAN GAS

1. THE STATOIL-INSPIRED PROPOSAL TO LAND NORWEGIAN STATFJORD GAS IN WESTERN NORWAY NOW SEEMS MORE SERIOUS THREAT THAN CONTINENTAL COMPETITION TO BRITISH GAS CORPORATION EFFORTS TO BUY THIS GAS. DELAY IN ANNOUNCING HMG'S APPROVAL OF THE BGC/MOBIL PLANS FOR A BRITISH GAS GATHERING LINE (A SINE QUA NON OF THE BGC OFFER) MAY CAUSE THE NORWEGIANS TO GO FOR THE STATOIL INSPIRED PROPOSAL. BGC'S ABILITY TO OFFER A MORE ATTRACTIVE WELLHEAD THAN THE CONTINENTALS WOULD THEN BE IRRELEVANT.
2. THE ECONOMIC PENALTIES WHICH THE NORWEGIANS WOULD HAVE TO PAY IF STATFJORD GAS WERE PIPED EXPENSIVELY ACROSS THE NORWEGIAN TRENCH TO A ROCKY LANDFALL IN WESTERN NORWAY SHOULD NOT BE SEEN AS NECESSARILY OUTWEIGHING THE NOW WIDELY-PERCEIVED POLITICAL ATTRACTIONS OF SUCH A PROJECT, WHICH IS TECHNICALLY FEASIBLE. THERE WOULD BE CONSIDERABLE NON-QUANTIFIABLE BENEFITS IN TERMS OF EXPERIENCE AND TECHNOLOGY OFFSHORE AND ONSHORE. THE EFFECT ON EMPLOYMENT DURING CONSTRUCTION AND THEREAFTER IN A REGION WHERE JOBS ARE SCARCE WOULD BE SIGNIFICANT. A PETRO-CHEMICAL COMPLEX IN WESTERN NORWAY BASED ON STATFJORD NATURAL GAS LIQUIDS (NGLS) SHOULD BE A COMMERCIAL SUCCESS. ONE SUCH COMPLEX (USING NGLS SEPARATED FROM EKOFISK CRUDE AT TEESIDE AND SHIPPED BACK TO NORWAY) ALREADY EXISTS AND IS PROFITABLE AT BAMBLE ON THE OSLO FJORD. TURNING THE REMAINDER OF THE STATFJORD GAS STREAM WHICH COULD NOT BE USED AS FUEL SINCE THERE IS NO MARKET IN NORWAY INTO METHANOL, AMMONIA, AND LIQUEFIED NATURAL GAS FOR EXPORT SEEMS UNLIKELY TO BE PROFITABLE BUT COULD PERHAPS BE JUSTIFIED AS PILOT PROJECTS TO PROVIDE A NORWEGIAN BASIS FOR MUCH BIGGER DEVELOPMENTS WHEN THE MUCH LARGER QUANTITIES OF NORWEGIAN GAS KNOWN TO EXIST SOUTH OF 62 DEGREES NORTH AND BELIEVED TO EXIST NORTH OF 62 DEGREES NORTH ARE BROUGHT ASHORE. THE NORWEGIANS CAN WELL AFFORD TO FINANCE THE PIPING OF STATFJORD GAS TO NORWAY AND ASSOCIATED PROJECTS, THE SUBMISSION OF WHICH TO THE STORTING NEXT SPRING WOULD BE ADVANTAGEOUS TO THE MINORITY LABOUR GOVERNMENT'S PROSPECTS IN THE GENERAL ELECTION TO BE HELD IN SEPTEMBER 1981.
3. AGAINST THIS BACKGROUND THREE ACTIONS BY HMG WOULD IN MY VIEW MATERIALLY, PERHAPS DECISIVELY, ASSIST BGC'S EFFORTS TO BUY NORWEGIAN STATFJORD GAS AND INDEED SUBSEQUENT TRANCHES OF NORWEGIAN GAS. ALL THREE INVOLVE CONSIDERATIONS WHICH ARE OUTSIDE MY FIELD. I HOPE HOWEVER THAT MY ASSESSMENT OF THE EFFECT UPON THE NORWEGIANS WILL BE TAKEN INTO ACCOUNT WHEN DECISIONS ARE TAKEN.

/4. THE

CONFIDENTIAL

4. THE FIRST AND MOST IMPORTANT IS AN EARLY FORMAL ANNOUNCEMENT BY BRITISH MINISTERS THAT THE GAS GATHERING LINE PROPOSED BY THE BGC/MOBIL STUDY TEAM HAS BEEN APPROVED AND IS TO GO AHEAD. THE NORWEGIANS KNOW THAT THE TIMING OF THIS PROJECT IS TIGHT AND THAT THERE HAS ALREADY BEEN SLIPPAGE. THE NORWEGIANS ARE ALREADY DUBIOUS ABOUT BRITISH ABILITY TO COMPLETE IT IN TIME TO TAKE STATFJORD GAS IN 1985. SUBSTANTIAL ALTERATIONS OF THE BGC/MOBIL PLAN WOULD CERTAINLY REINFORCE THESE DOUBTS. THE LONGER AN ANNOUNCEMENT IS DELAYED THE MORE LIKELY THE NORWEGIAN GOVERNMENT ARE TO GO FOR LANDING STATFJORD GAS IN WESTERN NORWAY SINCE THEY WOULD HAVE CONTROL OVER AS WELL AS RESPONSIBILITY FOR ANY DELAYS WHICH COULD RESULT IN LARGE SCALE AND POLITICALLY UNACCEPTABLE FLARING OF STATFJORD GAS. IDEALLY SUCH AN ANNOUNCEMENT SHOULD BE MADE NOT LATER THAN MID JUNE 1982 IN ORDER TO GIVE THE NORWEGIANS TIME TO CONSIDER THE IMPLICATIONS BEFORE OIL MINISTER GJERDE VISITS LONDON ON 16/17 JULY FOR DISCUSSIONS WITH MR HOWELL.

5. SECONDLY NORWEGIANS SHOULD BE INVITED TO TAKE A SHARE IN THE EQUITY OF THE BRITISH GAS GATHERING PIPELINE AS SOON AS OR INDEED BEFORE THE OFFICIAL ANNOUNCEMENT IS MADE. THE NORWEGIAN AUTHORITIES DISLIKE THE IDEA OF PIPING NORWEGIAN FETROLEUM THROUGH LINES OVER WHICH THEY HAVE NO CONTROL. THEY DO NOT CONSIDER GOVERNMENT REGULATION OF TARIFFS TO BE EFFECTIVE. NORWEGIANS WOULD PRESUMABLY WISH TO PARTICIPATE THROUGH STATOIL WHICH HAS ALREADY EXPRESSED TENTATIVE INTEREST. NORWEGIAN PARTICIPATION WOULD BE HELPFUL IN KEEPING TARIFFS DOWN TO A LEVEL GIVING SUITABLE BUT NOT EXCESSIVE RETURN ON CAPITAL INVESTED, IN KEEPING PIPELINE FULL, AND - IF PARTICIPATION COULD BE ARRANGED EARLY ENOUGH - IN ADVISING ON LOCATION/SIZING OF THE LINE SO AS TO PICK UP ADDITIONAL NORWEGIAN GAS THAT MAY BE ON OFFER LATER. FUNDING OF NORWEGIAN EQUITY SHARE RELATED TO NORWEGIAN SHARE OF THROUGHPUT WOULD PRESENT NO PROBLEMS. SUCH INVESTMENT IN OVERSEAS ASSETS CONNECTED WITH NORWEGIAN RESOURCES COULD BE POLITICALLY MORE ATTRACTIVE THAN USING SURPLUS ON CURRENT ACCOUNT EXPECTED THIS YEAR AND THEREAFTER ONLY TO REPAY ACCUMULATED OVERSEAS DEBT AND LESS INFATIONARY THAN SPENDING THE MONEY IN NORWAY.

6. THIRDLY BRITISH AUTHORITIES SHOULD OFFER TO ASSIST NORWEGIAN FIRMS INTERESTED IN PROCESSING NGLS FROM NORWEGIAN STATFJORD GAS IN BRITAIN REPRESENTATIVES OF SAGA PETROKJEMI WILL BE VISITING CROMARTY EARLY IN JUNE WITH THIS IN MIND. OSLO TELNO INDUS 5 OF 27 MAY TO DEPT OF INDUSTRY REPEATED TO DEPT OF ENERGY AND FCO. REFERS. NORWEGIAN AUTHORITIES WILL PROBABLY INSIST THAT WHEREVER THE STATFJORD GAS IS LANDED THE NGLS ARE BROUGHT BACK TO NORWAY FOR USE AS FEEDSTOCK. BUT SAGA ARE LIKELY TO MAKE GOOD USE OF COMPARISONS BETWEEN UK AND NORWEGIAN PLANS AND COSTS TO HELP ARGUMENTS OF THOSE NORWEGIANS WHO HAVE DOUBTS ABOUT PIPING STATFJORD GAS TO NORWAY.

LAMB

[THIS TELEGRAM WAS NOT ADVANCED]

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JS  
cc N10  
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10 DOWNING STREET

From the Private Secretary

20 August, 1979

Dear Mr Ward

You wrote to me on 9 August requesting that the Prime Minister receive a deputation from the Belfast City Council to discuss the Government's decision about a natural gas pipeline to Northern Ireland.

The Prime Minister recognises the significance of the decision for your Council and your wish to discuss it urgently with the Government. The matter is, however, primarily one for the Secretary of State for Northern Ireland and the Parliamentary Under Secretary of State (Mr. Shaw) who has responsibility for energy matters in Northern Ireland.

Mrs. Thatcher has therefore passed your request for a meeting with the Government to the Secretary of State and Mr. Shaw.

Yours sincerely

Michael Pitts

C. Ward, Esq.

out

PRIME MINISTER

Gas Pipelines

You raised two questions about North Sea gas pipelines.

First, you said that you had heard that the pipeline from Brent to St. Fergus was not operating because of environmental objections. This is not strictly so, though objections to other developments may indirectly restrict the extent to which the gases from Brent can be used. The position is as follows.

A separation plant is currently being built at St. Fergus. This plant will separate the various gases coming along the Brent line - i.e. methane, ethane, propane and other gases going up to C7. The methane will be fed into the BGC grid; the other gases will, it is hoped, be fed through another line to Mossmoran further down the coast where an LPG liquifaction plant and ethylene cracker are planned. Until the separation plant is completed, the Brent pipeline cannot operate.

However, although there will be no problem in feeding the methane from Brent into the BGC grid, there may be difficulties in using the other gases. The planning application for the pipeline to carry them to Mossmoran is at present on ice because of environmental objections; likewise, the two plants at Mossmoran are being held up because of environmental problems.

Even if these planning applications get the go-ahead, there will still be several years' time lag before Mossmoran comes on stream. During this period, the oil companies are planning to send the heavy gases to the Peterhead power station and to Cruden Bay where they can be liquified and "spiked into" the oil coming from the Forties Field and going on to Grangemouth. Two temporary pipelines from St. Fergus are planned for this purpose; the planning applications are currently being considered, and there are - as far as we know - no environmental objections.

/Second,

Second, you asked that the capital cost of the new gas gathering pipeline should not fall on the PSBR. We are of course some way from the capital stage: all that Mr. Howell has suggested for the moment is a further study. However, assuming it is decided to proceed with the project, this would almost certainly be implemented by the oil companies and not by BGC. If BGC were to undertake the project, then this would inevitably affect the PSBR - even if it only meant a smaller financial surplus for BGC. This of course is an argument for making sure that the private companies undertake the project.

12.

9 July 1979



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

R 2/7

The Rt. Hon. George Younger, TD MP  
Secretary of State for Scotland  
Scottish Office,  
Dover House,  
Whitehall,  
LONDON, SW1.

9 July 1979

*Sea Serv*

STUDY OF NEW GAS GATHERING PIPELINE IN THE NORTH SEA

I am grateful for your letter of 4 July and Keith Joseph's of 5 July.

Because of the onshore planning implications, the success of the project is very dependent on full and enthusiastic co-operation from your Department just as a successful project will bring major industrial benefits to Scotland. I entirely agree that your officials should keep in close touch with mine during the progress of the study and give all the assistance they can. I share Keith's concern that the study should take full account of the interests of all those who would benefit from bringing the gas ashore and look for help to your two Departments in this.

On Keith's second point, I am clear that if the study shows a new pipeline to be viable, Ministers will have to take speedily major decisions on the financing and organisation of the project. Those decisions will have to provide both for a strong central management of construction and operation and safeguard as much as possible a very large number of interests. I have at present no proposals for reconciling those two objectives. I think it would be useful to see what we can learn from the experience of other countries which have mounted projects of similar complexity and have asked my officials to investigate this experience. Meanwhile Mobil has not sought a commitment to its involvement beyond that proportionate to its share of the gas that would be transmitted through the new line.

I am copying this letter to Keith Joseph and the other recipients of yours.

*David*

D.A.R. Howell



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

01-211 6402

2  
Original filed  
Energy (Comm Book) May '79

6 July 1979.

Tim Lankester Esq.,  
Private Secretary to the Prime Minister,  
10 Downing Street,  
London SW1.

Prime Minister  
You agree this  
report should  
be published.  
R.

Dear Tim,

DEVELOPMENT OF THE OIL AND GAS RESOURCES OF THE UNITED KINGDOM, 1979.

The Annual Report on the development of the United Kingdom oil and gas resources (the 'Brown Book'), to which John Arnott referred in his letter to you of 30 May, is now ready for publication and I enclose an advance copy. Presentation to Parliament will be on 10 July by means of an arranged Parliamentary Question.

I am sending copies of this letter to the Private Secretaries of all Ministers on "E" Committee, and also to the Secretaries of State for the Environment, Defence, Scotland and Wales; and to Martin Vile (Cabinet Office).

Yours sincerely,

Bill

W.J. Burroughs,  
Private Secretary.

Encl.

Tim: - on one of  
our lines. someone  
- I can't remember who - told  
me that the gas we  
burn to show would not  
spend - because of environment  
objections. If it could, it  
could get more gas. Is  
this so? mff



Secretary of State for Industry

DEPARTMENT OF INDUSTRY  
ASHDOWN HOUSE  
123 VICTORIA STREET  
LONDON SW1E 6RB

TELEPHONE DIRECT LINE 01-212 3301  
SWITCHBOARD 01-212 7676

5 July 1979

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

R 517

Dear David,

STUDY OF NEW GAS GATHERING PIPELINE IN THE NORTH SEA

Thank you for sending me a copy of your letter of 2 July to George Younger.

I agree that it is appropriate to commission a new study of a pipeline and I am content with the terms of the proposed Parliamentary answer.

However, I should like to make two comments on issues which you have left open. First, I am concerned that the study should take full account of the interests of all those who would benefit from bringing the gas ashore. You say that the study will have to look at onshore facilities, but it is important that it should not do so solely from the point of view of Mobil/BGC.

Second, I attach importance to letting other companies with an interest in the pipeline play a part in the next stage if it is decided to go ahead with the project. There should be no question of permitting Mobil to establish a pre-emptive position at this stage.

I hope you will be able to reassure me on these points.

I am copying this letter to recipients of yours.

Yours,  
Kevin



SCOTTISH OFFICE  
WHITEHALL, LONDON SW1A 2AU

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

R  
5/7  
4 July 1979

Thank you for your letter of 2 July about your intention to make an announcement tomorrow about a study of a new gas gathering pipeline in the North Sea.

I am greatly encouraged that such a study is being arranged recognising the need for optimum use to be made of North Sea resources. This applies with special force to the NGLS on account of the downstream possibilities they offer us onshore. As you mention in the light of not only of the national but also the specifically Scottish interests in such a study, I suggest that it would be helpful to all concerned if my officials were to keep closely in touch with yours during the progress of the study.

I am copying this letter to the recipients of yours.

GEORGE YOUNGER



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

*Prime Minister 2*

*To note - a new  
 study of a gas  
 gathering pipeline  
 to be commissioned.  
 other ministers welcome  
 this.*

CONFIDENTIAL

The Rt. Hon. George Younger, MP  
 Secretary of State for Scotland,  
 Scottish Office,  
 New St. Andrews House,  
 EDINBURGH.

*Dear George*

*New phase The capital cost must  
 not come on the  
 PSBR. See comment  
 cluster on another & June 1979  
 Road pipeline 5/7*

STUDY OF NEW GAS GATHERING PIPELINE IN THE NORTH SEA

You will recall that last year the previous Administration received a report by Gas Gathering Pipelines (North Sea) Ltd (GGP) which concluded that the associated gas expected to arise in the UK sector of the northern North Sea could be accommodated in the existing pipelines to shore. That conclusion was finely balanced and subject to a number of uncertainties.

Since the GGP report there have been a number of developments. We now have a better knowledge of the likely size and timing of UK gas availability, and it has become clearer that much of the gas expected to arise may be of a quality unsuited to the existing pipeline and terminal facilities. The needs of the British Gas Corporation (BGC) to secure more supplies from the mid 1980s to meet expected demand have become better defined. We are now increasingly confident that UK gas reserves would justify a new pipeline, indeed that a new line will be necessary if we are to avoid flaring substantial quantities of gas in the second half of the coming decade.

There is also the Norwegian element. Unsuccessful attempts have been made for some years to get the Norwegian Government to co-operate on a joint gas gathering project. They continue to hold back, but it now looks likely that they will have to decide on gas sales from the median line Statfjord field quite soon, and that the UK might be the favoured customer. Securing the Norwegian share (nearly 90%) of Statfjord gas would be a major prize, and to do so by way of a new pipeline running parallel to the median line for some distance would mean that we were well placed to receive also all subsequent tranches of Norwegian gas from the northern part of their Shelf. Without such a line the danger is that the Norwegians will succeed in putting together enough gas to justify a "spine line" running all the way to the Continent. This would suck in all Norwegian gas and, I fear, expose us to pressure to make available some UK gas arising close to the median line.



CONFIDENTIAL

The final impetus for a new look arose when Mobil indicated that it was considering an application for authorisation to construct a pipeline to transport gas from its Beryl field to the UK. I have therefore invited Mobil Oil Corporation and BGC jointly to conduct a study of a new gas gathering line in the northern North Sea. The two Corporations have now agreed to draw up specifications for and then to carry out a study of such a line. This will cost something around £1M, which will be borne by Mobil and BGC.

Subject to the receipt of satisfactory assurances from Mobil about the resources they will commit to it, I propose to announce the study on Thursday 5 July by way of an arranged PQ; I attach a copy of the text so that you are forewarned.

The gas which would be landed in any new line would probably be rich in NGL. The study will therefore need to look at the onshore facilities required to handle this NGL - pipelines, fractionation plant, and harbours. The quantity of ethane coming ashore is likely to be at least sufficient to provide feedstock for a "world size" ethylene cracker. In view of the difficulties at Mossmorran, which we all hope will soon be satisfactorily resolved, this may well be one of the most important parts of the study's work, and the most difficult part of any subsequent pipeline project. But it offers the prospect of major new industrial investment in Scotland.

A lot of new gas is expected to be available for collection in 1984/85. If there is to be a new pipeline, there is no time to be lost; indeed we are already a year behind the ideal timetable. I have therefore stressed to Mobil and BGC the need to complete the study as quickly as possible, and I hope it will be ready early next year. I have, of course, left completely open the questions that will arise should the study recommend that a new line be built, namely who should construct, own and operate the line, and who should provide the finance (Mobil have in fact offered to finance at least that proportion of the project attributable to their own gas, and BGC have expressed interest). However when we have the study we shall have to respond speedily to its recommendations. My officials will be monitoring the progress of the study, and as soon as the results begin to emerge we shall need to start addressing ourselves to the important decisions which will be required.

I am sending a copy of this letter and proposed announcement to the Prime Minister, colleagues on 'E' Committee, and Sir John Hunt.

D.A.R. HOWELL

*David*

DRAFT



✓ MA 30/6

Q: To ask the Secretary of State for Energy what consideration is being given to a new gathering pipeline to bring ashore gas from the Northern Sector of the North Sea?

A: Mobil North Sea Ltd has indicated that it is considering the construction of a gas pipeline to transport gas to Great Britain from Block 9/13A which includes the Beryl field operated by Mobil. At my request it has discussed with the British Gas Corporation (BGC) the possibility of designing the line to accommodate other gas of the quantity and quality expected to be available in the Northern Basin of the North Sea from the mid 1980s. British Gas and Mobil have now agreed to draw up jointly specifications for a feasibility and design study of such a project and to carry out the study as quickly as possible.

The study will concentrate on gas which is likely to arise around a line running South from Quadrant 211 to the area of Quadrants 15 and 16 then Westward to the Scottish coast. But it will consider also other gas likely to arise North of the 56th parallel. Although preliminary indications are that a new gas line will be required, the study will also consider whether this gas might be accommodated in the existing pipeline systems. The operators of those systems have assured me of their cooperation. I also look to the licensees of fields which might feed gas into a new line to cooperate fully both in discussions of the gas reserves which might be available and of the platform



facilities which would be relevant to their collection.

*Natural Gas Liquids*

The indications are that the new gas to be landed will be rich in ~~gas~~. The study will therefore need to consider the requirements for additional onshore pipelines, gas processing, and harbour facilities to handle the NGL which would include at least sufficient ethane to meet the feedstock requirements of an ethylene cracker.