

CC Master
Energy Broc P2

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OIL POLICY

NOTE OF A MEETING HELD AT 10 DOWNING STREET AT 2:30PM ON
FRIDAY 21 DECEMBER 1979.

PRESENT: THE PRIME MINISTER
THE CHANCELLOR OF THE EXCHEQUER
THE LORD PRIVY SEAL
SECRETARY OF STATE FOR ENERGY
ATTORNEY GENERAL
SIR KENNETH BERRILL

MR P LeCHEMINANT)
MR P MOUNTFIELD) Secretaries

1. GOVERNMENT-TO-GOVERNMENT OIL SALES

The meeting considered a note by the Secretary of State for Energy circulated with his Private Secretary's letter of 20 December.

THE SECRETARY OF STATE FOR ENERGY said that he wished to take the opportunity of his visit to the Middle East early in January to explore the possibility of Government-to-Government oil purchases. As agreed at the Prime Minister's meeting on 10 December, he had arranged for informal discussions with BP and Shell. While neither company was enthusiastic about the prospect, both recognised that in present circumstances, an increasing proportion of oil sales were likely to take the form of Government-to-Government deals, but were anxious that any initiatives taken by the British Government should not undermine their position in those countries where they still had a significant stake. The oil companies were anxious to be kept in touch.

In discussion, there was broad agreement that the British Government could not afford to ignore the possibility of such oil sales in future. At the same time it was important not to damage the interests of our own oil companies. We should therefore concentrate on developing

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Government-to-Government contacts with those countries where BP and Shell no longer had a significant interest. It was also important that BNOC, if it were used as an instrument in these sales, should not be put into a position where it might make sizable losses.

THE PRIME MINISTER, summing up the discussion, said that the meeting agreed the Secretary of State for Energy should explore, on an entirely non-committal basis, the possibility of Government-to-Government sales, and should inform her of the reactions here received.

2. PRIVATISATION OF BNOC.

The meeting considered a note by officials, circulated under cover of a letter from the Chancellor of the Exchequer's Private Secretary dated 20 December.

THE CHANCELLOR OF THE EXCHEQUER said that he hoped to raise £500 million by way of disposal of public sector assets in 1980-81. About half of this was already available from 'firm offers'. Or a number of other potential sales, and it would not be absolutely necessary to dispose of part of BNOC in order to meet the target. But BNOC could make a significant contribution. The figures in the paper set out first, the contribution which BNOC's cash flow was likely to make to a reduction of the public sector borrowing requirement (PSBR) over the years to 1983-84. It then showed, for each of four possible disposal cases, the difference which this would make. Consistent assumptions about the future course of oil prices had been taken, and tax revenue was shown separately. The essential difference was that any sale of assets involved giving up future revenues in exchange for immediate cash. The Budgetary position in 1980-81 and 1981-82 would probably justify such disposals. The longer-term objective remained the privatisation of large parts of the present public sector.

In discussion, it was suggested that the Government might need the additional revenue from BNOC just as badly in the later years of the

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period. If oil prices continued to rise in real terms at their present rate, those revenues would be significantly higher. It might be more prudent, therefore, to dispose of a comparatively small part of BNOG in the early years.

In further discussion, it was argued that any split of the existing BNOG into a 'trading' and 'operating' subsidiary would be seen overseas as a political device intended to retain a Government control over the destination of North Sea oil. Against this it was argued that the proposed arrangements were easier to defend, in terms of community law, than the present participation deals, which contained 'sale back' arrangements which were open to challenge. On balance, it seemed that, internationally, there was nothing to lose and possibly something to gain from the proposed changes.

It was further argued that the device of splitting the present BNOG would weaken the management of the BNOG 'trading' subsidiary by depriving it of information about the costs of North Sea oil production. Most major oil companies still operated as integrated entities, combining production with trading functions. Against this, it was argued that BNOG 'trading' would be dealing with many different production companies, and there was no particular case for it to retain a stake in its former affiliate, BNOG (operating). Indeed the operation might go better if the two were at arms length.

In continuing discussion, it was suggested that the sales of the 'operating' subsidiary would command a better price if it were made clear to the market from the start that the ultimate objective were to remove the new company from Government control. This would also have the technical advantage of removing the company from the public sector, and thus allowing the proceeds of sale to be treated as a reduction of the Public Sector Borrowing Requirement, rather than a means of financing it. It was however suggested that the accounting conventions in this area were unnecessarily rigid and need not be regarded as an overriding objection.

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THE PRIME MINISTER, summing up the discussion, said that the meeting agreed on a division of BNOC into separate 'operating' and 'trading' subsidiaries. The necessary legislation should be drafted accordingly. While the ultimate object remained the privatisation of BNOC, there was no need for a decision at this stage on the timing, speed or extent of disposal of shares in BNOC (Operating). The Secretary of State for Energy, in consultation with the Chancellor of the Exchequer, should raise the issues again at a later stage. At the same time, the Chancellor of the Exchequer should re-examine the accounting conventions which determined whether or not the proceeds of sale counted as a reduction of the PSBR.