

Prime Minister



Treasury Chambers, Parliament Street, SW1P 3AG

01-233 3000

PRIME MINISTER

THE GOVERNMENT AND BANK OF ENGLAND HOLDINGS IN BP

You should be aware of two matters concerning the Government and Bank of England holdings in BP on which decisions are necessary. They are:

i) The then Deputy Governor proposed that he should hold a secret exploratory discussion with Sir Alastair Down, Chairman of Burmah, to find out the sort of figure at which his Company's action with the Bank might be settled out of Court. Further details are in the Sir Jasper Hollom's note attached. The Attorney General's advice on the proposal is in his letter of 20 February, also attached.

ii) Sir David Steel, Chairman of BP, has warned us that BP may well wish to use its unused authorised share capital for the purpose of making acquisitions. This would dilute the Government's holding in the Company.

2. The Burmah Action against the Bank of England

The amounts at stake in the action are very large. The memorandum attached to Sir Jasper Hollom's letter puts the difference between the cost of the shares and their revaluation on 29 November at over £1,000m (the share price has risen since then) and dividends received on these shares

Are you content with the Chancellor's conclusions?

(Mr Howell has agreed them).

I think both are right, but you might like to discuss the Burmah question with the Chancellor before reaching a final view.

R

12/3

[Douglas
Cross is seeing
David
Steel
this
morning;
it would
be
helpful
if he
could
tell
him
on
decision
on the
BP
question]

020
I must leave the chairs
entirely to the Chancellor.
I can give no advice because this
was one an employee of Burmah
& is still on the Board &
of its subsidiaries.
Mrs.



since their acquisition, which Burmah are also claiming, amount to approximately £100m. They are also seeking an unquantifiable amount of damages.

3. The enormity of these sums suggests that if there were doubts about the soundness of the Bank's legal case, it would be no more than prudent to safeguard our interests by seeking a reasonable settlement. But there is clear legal advice that Burmah do not have any real prospect of success. Obviously this does not guarantee success in the Courts, but there is nothing in the legal advice which suggests that we should pay substantially for an out of court settlement with Burmah.

4. The cost of a settlement would be high. Sir Jasper Hollom's guess is in the order of £75m-£100m. The Attorney doubts whether any settlement could be achieved for less than £100m. I agree. The Attorney says in his letter that we cannot appear to refuse to consider any suggestion from Burmah for some minimal settlement and suggests that any such proposal at a figure around £5m could well be considered as worthwhile for disposing of the action. It seems inconceivable that Burmah would agree to a settlement on these terms in view of the vigour with which they have pressed the action, the amounts at stake, and the pressure upon them from the Burmah Shareholders' Action Group. Indeed, the only way in which Sir Alastair could present a settlement of £5m to his shareholders would be by a frank admission that despite previous statements, their legal advice was that their action was not well founded (a line of argument which would make it harder for us to explain why we had agreed to settle at this figure).



5. There are no present plans for a sale of BP shares. If such a sale was ever contemplated, it would be more easily done if the former Burmah holding was firmly in the Government's hands brought about by the early settlement of the action. The Government's shareholding would then be 45.7 per cent (before taking account of the changes referred to in paragraphs 7 and 8 below). This is well above the 25 per cent holding necessary to be certain of blocking special resolutions amending the provisions in the Company's Articles giving the Government the right to appoint two directors with powers of veto etc. (In practice, a somewhat lesser holding should be sufficient to block such resolutions.) But as I said earlier, we have no plans for a further BP share sale and our advice is that Burmah do not have any real prospect of success in their action. I therefore do not think that the possibility of a further sale of BP shares is a factor which ought to be taken account of in our decision on Sir Jasper Hollom's proposal.

6. My conclusion from this is that it would only be worthwhile authorising the Bank of England to have exploratory discussions with Sir Alastair if the Government were willing to pay out some £100m and perhaps more for a settlement. The payment could not be concealed. It would appear on the Treasury Vote and would represent a claim on the Contingency Reserve. Bearing in mind the firmness of the legal advice (which, as the Attorney mentions in his letter, is known to his predecessor) I do not think this could be justified. I therefore propose to tell the Bank that - to use the words in the penultimate paragraph of his note - since Ministers feel that they must anyway rule out a settlement which involved a substantial payment to Burmah, we would not want them to undertake the exploratory discussions with Sir Alastair Down.



7. The use of BP's Unissued Authorised Share Capital
Sir David Steel has told us that although BP have no plans at present to make acquisitions through the issue of new shares, the Company may wish to do so at any time in the future. Indeed, we understand that they are considering purchasing a UK company, worth around £200m, as part of their diversification into the minerals sector. The purchase would be financed by the issue of shares from BP's unused authorised share capital.

*Cent. we
buy sufficient
to keep H.M.G.
holding above
20%
for obvious
reasons.*

8. The effect would be to dilute the Government's holding in BP as follows:

(i) The issue of all BP's unissued authorised share capital would reduce the Government's holding to 20.33 per cent. The issue of sufficient shares to finance a £200m acquisition would reduce the holding to some 24.7 per cent.

(ii) The undertaking with the Take Over Panel not to vote the Bank's holding effectively sterilises the Bank's shareholding in the Company. Thus, excluding the disenfranchised Bank holding, HMG's voting share of the Company, assuming the issue of all the unused authorised share capital, would be 24.18 per cent, and assuming the issue of shares to finance a £200m acquisition, 30.63 per cent. The Bank would very much support any proposal to re-enfranchise their share and would support an approach to the Take Over Panel. But they advise that an approach ought to be deferred until say a year has elapsed since the share sale; ie until next November.



(iii) Re-enfranchisement of the Bank's shares would, assuming issue of all the unused authorised share capital, give HMG and the Bank a combined holding of 36.26 per cent and some 44.05 per cent if shares were issued to finance a £200m acquisition.

9. Thus, provided that the Bank are successful in defending the Burmah action, the issue of all BP's unused authorised share capital, let alone enough to finance a £200m acquisition, would not bring the combined public sector holding to anywhere near the 25 per cent limit. If the Burmah action is lost, the holding slips below 25 per cent.

10. I do not think that we should object to the use by BP of their unused share capital to finance acquisitions. It is in the national interest that BP should carry through a successful programme of diversification. Moreover, if they do not finance acquisitions through share issues, they would presumably do so by cash payments. This could require a rights issue which, if the Government were to subscribe, would add to public expenditure. Furthermore, any attempt to stop them, which might not succeed, would be inconsistent with the Government's traditional policy of non-intervention in the Company's commercial affairs - this hardly seems a case for the use of the Government directors' veto.

11. My conclusion therefore is that we should tell the Company that we have no objections to their using their existing unused authorised share capital to finance acquisitions, but we would want to be consulted before there was any proposal to increase the present authorised share capital.



12. I should be glad to know that you agree with my approach to these two matters.

13. I am sending a copy of this minute to the Secretary of State for Energy and to the Attorney General.

A handwritten signature in dark ink, appearing to be "G.H." with a flourish.

(G.H.)

6 March 1980

Q. "TO ASK THE SECRETARY OF STATE FOR ENERGY WHAT PLANS HE HAS FOR THE FUTURE OF THE BRITISH NATIONAL OIL CORPORATION?"

- A. I will be introducing legislation as soon as Parliamentary time permits in the new session to allow for the setting up of a company through which the British public will be able to invest in BNOC's offshore operations.
2. BNOC has two distinct functions. First its access to oil through the participation and royalty in kind arrangements gives it an important role as a large scale oil trader. In this role BNOC can play an important part in protecting vital national interests including security of supply and in providing oil supplies for our international partners in the EEC and IEA. We intend that this role should continue.
 3. Second, BNOC is an oil producing company working alongside other oil companies in the North Sea. We see no need to retain these operations within the State sector and we shall therefore give the public the chance to participate directly in BNOC's oil producing business.
 4. We have therefore decided that BNOC should be re-organised. The existing Corporation will concentrate on oil trading. The participation agreements which give BNOC options to take oil will be retained, and I will continue to call upon BNOC to dispose of royalty oil on my behalf.
 5. The exploration and production assets and operations will be vested in a new Companies Act company. We intend that this company will operate independently of Government and of BNOC, except to the extent that its UKCS oil will be subject to purchase options by BNOC under normal participation arrangements. We propose to make a substantial shareholding in the company available for issue to the general public. The Government will not seek to control the company through the residual public sector holding of the shares - which it is intended will ultimately be reduced to a minority.

2.

6. The Government wishes to see a wide spread of ownership and will ensure that in the allocation of shares full regard is given to the position of small investors and employees.
7. Implementation of these proposals will call for a major corporate re-organisation and for the transfer of contractual and other interests. This is bound to take time. But preparatory work on this and on the necessary legislation is underway. The timing of the share issue will be a matter for further consideration.
8. These proposals will result in a proper separation of BNOC's two functions of oil production and of oil trading. We will thereby provide a secure foundation for further development of the United Kingdom Continental Shelf in the national interest.

Department of Energy
6 March 1980

The Burmah Action against the Bank of England

The origins of this action, which lie in the rescue operation mounted by the Bank of England with the guarantee of HMG at the end of 1974 and early in 1975 for the greatly over-extended Burmah Oil Company, do not need to be set out in detail for the purposes of this note. It is enough to recall that the first rescue plan envisaged help by way of loans and guarantees, secured in large degree by the pledge of Burmah's holding of BP and Shell stock. This plan would, of course, have given to Burmah the benefit of any improvement in the price of the stock pledged. Hardly was this plan agreed, however, than Burmah came back to say that further examination of the obligations attaching to their existing borrowing commitments showed that, if they went through with the pledge of these stockholdings, they would breach various covenants and would be forced into liquidation. Since this would have crystallised their vast exposure on tanker charters, the company's collapse would have been total. Burmah accordingly proposed that the Bank should have no security whatever (the BP and Shell stockholdings remaining unencumbered in Burmah's hands) and should make an injection of some £225 mn. in effect in equity form. The Bank refused to contemplate such a one-sided arrangement and insisted that, if the BP stock could not be pledged, it must be sold; but they did hold out a hope that they might be able to agree to some form of profit sharing on any eventual appreciation in the value of the stock. The thinking behind this idea was that, since the original proposal would have given Burmah the full value of any appreciation, it was hard in the revised plan to deprive them of it

in toto. In the event HMG - whose guarantee was still essential to the whole operation - insisted, despite strong representations by the Bank and Burmah, that there should be no profit sharing provision and indeed that the stock should be purchased at something below the (by then rising) market price. In due course, Burmah issued a writ claiming the return of the stock, the dividends received thereon meanwhile, and damages.

Burmah, guided by Sir Alastair Down, has meanwhile made a notable recovery which has put it in a position where it is ready to make advance repayment of the \$100 mn. loans guaranteed by the Bank which are a remnant of the rescue operation and could also without difficulty do without the sterling standby which also remains in place. On the legal front, the interval has been largely filled by an attempt by Burmah to obtain disclosure of a large number of documents on which HMG claimed Crown Privilege. That case Burmah have lost successively in the High Court, the Appeal Court and the Lords and the main action is now scheduled to be taken in October 1981. Meanwhile, the prize over which the main action is to be fought has grown rapidly, the shares bought from Burmah in January 1975 for £179 mn. having risen in value by the time of the last revaluation on the 29th November to £1,201 mn. The shares being held in the Bank's Issue Department, the amount of the unrealised appreciation has, under the rather odd accounting conventions applied to that Department, been regularly paid over on the quarterly revaluation dates so that HMG has already received (and spent) the £1,000 mn. + of the profit.

The Bank maintain very close and friendly relations with Alastair Down which include discussions off the record, without prejudice, and indeed without the knowledge of the Burmah Board, about the dispute. Down recently said in one of these conversations that they had drawn a good deal of encouragement from the judgments delivered at the various levels in the Crown Privilege case, which he believed served to strengthen materially the hopes of his lawyers

about the eventual outcome of the main action. Nevertheless, he would much like to get rid of the action and would be willing to settle if he could get a reasonable offer. He made it clear that he would have to have something material to satisfy his Board and his shareholders (the hopes of the latter having been substantially fanned by the Shareholders Action Group). He stopped short, however, of indicating any order of magnitude that might be in his mind, declaring only that he would not be greedy and that he was confident he could deliver both his Board and his shareholders on a bargain to which he was prepared to put his hand.

The Bank have also reviewed with their Counsel the question of what clues to the fate of the main action can be drawn from the judgments in the Crown Privilege case. The Bank's Counsel remain extremely confident and say that they are substantially further encouraged by these judgments as they read them. The main action holds no embarrassment for the Bank, since action it took was taken at the insistence of the Government; nor presumably is there any embarrassment in the action to the present Administration. Nevertheless, the Bank would see virtue in a settlement if an acceptable basis could be found. The main reason for this is that, to the Bank, it still seems clear that it was inequitable to deny Burmah a share in a potential profit which events have shown to exceed £1,000 mn.; and it is further obviously undesirable to drag such an action through the Courts, at great cost, if it can be avoided. There are more productive things for both the Bank and the company to be doing and it is a pity to expose a Government, of whatever party, to the kind of comment that must be expected to flow.

On the other hand, the prospects of acceptable terms being found cannot be put very high. This is principally because the sums at stake are so vast and moreover both sides have loudly proclaimed their complete faith in the strength of their own case. Against such a background, any settlement would have to be large -- falling at a guess in the region of £75 mn.-£100 mn. The difficulties of agreeing in the face of present stringencies to a payment on such a scale are obvious.

It may well be therefore that, at the end of the day, we may have to conclude that a Court battle cannot be avoided. But before so deciding it would seem worthwhile at least to find out what sort of a figure Down has in mind. Down confirms that he would be willing not only to enter into a secret exchange with the Bank on this, of course without prejudice; but also to take the initiative in asking for it. On this basis there should be no embarrassment about an exploratory discussion, which it should anyway be possible to keep secret. Accordingly, unless Ministers were to feel that they must anyway rule out a settlement which involved a substantial payment to Burmah, the Bank would like to conduct such an exploration.

Burmah would be happy to disguise the scale of a settlement to some extent, for instance by wrapping it up in some way in a purchase of assets from BNOC. But such questions would be for a much later stage and it would be unwise to suppose that the true scale of any settlement could be readily much disguised.

4th January 1980.

SECRET



01-405 7641 Extn

ROYAL COURTS OF JUSTICE

LONDON, WC2A 2LL

CC MR RYRIE

20 February 1980

The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer
HM Treasury
Parliament Street
LONDON S W 1

CH/EXCHEQUER	
REC.	22 FEB 1980
ACTION	MR BRIDGEMAN
TOPICS	SIR D WASS
10	PS/EST
	PS/IST
	MR F. JONES
	MR MOWER
	MR COLLINSON

MR WICKS

MR RIDLEY

Dear Geoffrey,

My advice was sought on a number of points arising from a proposal put forward by the Deputy Governor of the Bank of England to settle the action brought against the Bank by Burmah.

I have considered the opinions of counsel which have already been obtained (one opinion was requested by, and is known to, my predecessor) and have found nothing which would persuade me to differ from the views already expressed. I do not think that Burmah have any real prospects of success against the Bank of England.

Bearing in mind Burmah's lack of prospects and one other important consideration, namely the obvious implications of the cost of any settlement given the present economic climate, I am reluctant to recommend such a course of action. I would doubt that any settlement could be achieved for less than £100m.

On the other hand, we cannot appear to refuse to consider any suggestions from Burmah for some minimal settlement. Any such proposal at a figure around £5m could well be considered as worthwhile for disposing of the action.

I think that it is important that the proposal for a settlement should not originate from the Bank because this could be interpreted as a lack of confidence in its case. I do not favour the creation of a team for the purposes of the negotiations but I do consider that it would be desirable that Senior Counsel for Burmah and the Bank should meet so that any proposals for settlement by Burmah can be considered.

However if this is not possible and that for reasons you will know about - negotiations must be conducted by the Deputy Governor on behalf of the Bank it must be made clear that his brief is to listen to any proposal and to report back. There should be no discussion by him of the merits nor any mention made of specific figures by him.

Yours W...

Michael



E-6 MAR 1960