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10 DOWNING STREET

From the Private Secretary

16 July 1979

Dear Sir,

Future of BNOC

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

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

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

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

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

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

Summing/

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

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

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Bill Burroughs, Esq.,
Department of Energy.

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Energy No 14

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10 DOWNING STREET

From the Private Secretary

18 July 1979

Future of BNO

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

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

- not "26% of the equity".

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

T. P. LANKESTER

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

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