



Energy

Treasury Chambers, Parliament Street, SW1P 3AG  
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4 February, 1980

Dear David

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BNOC FUTURE CAPITAL STRUCTURE

Thank you for your letter of 25th January which seeks approval for BNOC's future financial structure.

I am generally content with your proposals, subject to the following points.

(i) Scope of the New Corporation's Activities: I understand that the intention is to give the new Corporation exactly the same powers as are given to the existing Corporation by the 1975 Act; i.e. besides the power to carry on oil trading, which at the moment is the only function identified for the new Corporation, powers to explore for and develop petroleum all over the world, operate refineries etc. I understand that you do not see circumstances in which we would want the new Corporation to be more than an oil trader, but that you nevertheless want to keep the options open for the future.

I would not necessarily argue that the legislation should specifically restrict the new Corporation to oil trading, but I question whether it is right for it to be empowered to do everything that the old Corporation could. I should, therefore, be grateful if you could consider giving the new Corporation much more limited powers to suit the role we now see for it.

(ii) PDC: I am not convinced that PDC would be appropriate for the new BNOC since the risk must be that it would become soft option capital. Indeed, this appears to be recognised in paragraph 4 (i) of the note attached to your letter where it states that "it would be unrealistic to assume that BNOC would be able to remunerate such capital by fixed interest payments - equity therefore seems appropriate". This effectively accepts that on its main function, oil trading, the new Corporation will not be viable in that it would not be able to service its capital at the normal NLF rate. This also suggests that the Corporation would not be able to meet

The Rt.Hon.David Howell, M.P.





one of the criteria for PDC that "taking the good and bad years together, the average level of gross dividend payments would be at least as much as interest which the Government would have received if it had advanced the money from the National Loans Fund" (paragraph 86 of Cmnd 7131). The right course in circumstances where a nationalised industry is not viable is to provide for its trading losses to be met by grants from Parliament, and not by endowing it with soft capital.

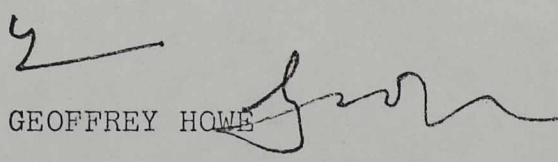
As I say, this makes me reluctant to agree to the inclusion of powers in the Bill for the provision of PDC, particularly if we decide that the Government rather than the new Corporation should own the public sector stake in Operating. I hope that you can, therefore, reconsider your proposal here. However, in view of the importance of enacting the legislation this session, I would not resist your proposal for the inclusion of powers in the Bill for PDC if you thought this essential provided other colleagues were content. The Treasury's position must, however, be reserved on the use of those powers to issue PDC.

(iii) Power to make Grants: I agree with your proposal that the Bill should contain a power to make grants to the Corporation out of money voted by Parliament, but I think that Parliament will expect that this power should be circumscribed in some way, e.g. by indicating the purposes for which the grant can be paid. An obvious way of doing this would be to stipulate that they should be paid with a view to reducing or eliminating the Corporation's deficits.

My officials are in touch with yours about some minor points on your proposals.

More generally, could I say that the note attached to your letter does indeed suggest that the new Corporation will be doubtfully financially viable. The note draws attention to the doubts that BNOC will be able to remunerate the capital for its main oil trading business by fixed interest payments and that while in normal circumstances it should have relatively small profits or losses, its trading operation entails by its nature a significant exposure to loss. I think that colleagues ought to be aware of these risks.

I am sending copies of this letter to the Prime Minister, John Nott, Keith Joseph and Sir Robert Armstrong. If John Nott and Keith Joseph see any inconsistencies in your proposals with their legislation now before Parliament, no doubt they will let us know.

  
GEOFFREY HOWE