

Energy

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PRIME MINISTER

Review of Depletion Policy

BACKGROUND

Discussion of depletion policy was postponed because the Attorney General advised that Ministers should not change their policy in the middle of the BP share sale. That problem has now passed, and the Secretary of State for Energy has taken the opportunity to update his earlier review and submit fresh proposals.

2. The report by officials attached to Mr. Howell's paper is a thorough piece of work, which is helpfully summarised on pages 1 to 6. Within the summary the specific recommendations made are to be found in sub-paragraphs (xiv), (xv), (xvi) and (xvii) on pages 3, 4 and 5. In his covering paper Mr. Howell endorses the report's recommendations and invites colleagues "to agree that we should be moving towards the policy of slower depletion in the 1980s". He wants permission to begin discussion with the oil industry about how the new policy could best be implemented. In the light of these discussions he would then propose to "advise my colleagues further on the timing and content of a statement we might make on our policy, bearing in mind the closeness of the EEC Council of Ministers' meeting at the end of March". In addition to these recommendations which are to be found in paragraph 6 of his covering paper, Mr. Howell also tucks away in paragraph 3 the proposition that the exploration effort on the United Kingdom Continental Shelf should be stepped up in order to "bear fruit in the 1990s".

3. There are four separate issues underlying Mr. Howell's approach:-
- (a) Should an effort be made, and if so by how much, to shave off the peak of production foreseen in the 1980s, in order to preserve oil for the 1990s?
 - (b) What instruments should be used to achieve any such shaving?
 - (c) What should be said?
 - (d) When should it be said?



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Section 100

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The first part of this section deals with the general principles of the law of contract. It states that a contract is an agreement between two or more parties which is legally binding and enforceable. The law of contract is concerned with the rights and obligations of the parties to a contract.

The second part of this section deals with the formation of a contract. It states that a contract is formed when the offer and acceptance are made. The offer must be made by a person who is capable of entering into a contract and the acceptance must be made by the person to whom the offer is made.

The third part of this section deals with the performance of a contract. It states that a contract is performed when the parties to the contract do what they have agreed to do. If a party fails to perform its obligations under a contract, it may be liable for damages.

The fourth part of this section deals with the termination of a contract. It states that a contract may be terminated in a number of ways, including by agreement, by breach, and by operation of law. The law of contract is a complex and important area of the law which is constantly evolving.

The fifth part of this section deals with the remedies available for breach of contract. It states that the law provides a number of remedies for breach of contract, including damages, specific performance, and rescission. The law of contract is a complex and important area of the law which is constantly evolving.

The sixth part of this section deals with the law of agency. It states that an agent is a person who is authorized to act on behalf of another person. The law of agency is concerned with the rights and obligations of the principal and the agent. The law of agency is a complex and important area of the law which is constantly evolving.

The seventh part of this section deals with the law of tort. It states that a tort is a wrongful act which causes harm to another person. The law of tort is concerned with the rights and obligations of the parties to a tort. The law of tort is a complex and important area of the law which is constantly evolving.

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4. Present versus future gains: if it were possible accurately to foresee the future price of oil and to establish the correct discount rate, decisions in this area would be largely a matter of arithmetic. But certainty is not available to us. The question therefore becomes - and it is neatly illustrated in Figure 4 of the report - whether we want a net gain to the balance of payments in the 1980s (and associated revenues to the Exchequer) more, or less, than we want two or three more years of "self-sufficiency" in the 1990s. There are two additional points to be made. First "self-sufficiency" in oil supplies is a comforting concept with little real meaning. We are, and will remain throughout the period, large importers and exporters of oil. It is meaningful to ask "how much money or foreign currency do we want to get from UKCS". It is not meaningful to view this amount in relation to our oil consumption because there is no question of absolute shortage - other than politically-motivated shortage - arising during the period. The second point is that the "re-entry" problem - i. e. the likely sharp increase in our net oil imports in the 1990s - is not eased by these depletion proposals - but merely postponed for two or three years.

5. Depletion techniques: there are five basic techniques available to us to restrain oil output: we can put limits on gas flaring; we can delay the start-up of new oil fields; we can refuse to allow companies to adjust their field production profiles upwards once they have been agreed; we can use our powers - from 1982 - to restrain the output from existing fields; and we can space out or bunch up the issue of new exploration licences. Comments on each are:-

- (a) Gas Flaring. On almost any assumption it makes economic sense to restrain the burning off of associated natural gas as far as the technicalities allow. Gas burnt is lost forever. The recommendation by officials that we should adopt a 'tight' approach to proposals for gas flaring, makes sense.
- (b) Upward Profile Variations. Officials say, rightly, that Government action to refuse upward profile variation on individual oilfields can be defended only against the background

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of a stated policy of restraining production. Decisions here therefore are a consequence of the basic decision on whether to seek to defer oil production from the 1980s to the 1990s.

- (c) Development Delays. This is a tricky area because unwarranted delay could result in complaints of Government mismanagement. Colleagues may feel that there should be a bias against unnecessary delay rather than, as the report suggests, in favour of taking our time.
- (d) Production cut-backs. This is the key element in any conscious depletion policy and the one most fraught with difficulty. The oil companies would loathe it because it defers production of the most profitable oil from each field and has a direct effect on finance and profits (as well as on tax and balance of payments flows). It can also run into technical troubles - e.g. it can run counter to "good oilfields practice". This is the element which is most affected by - and bears on - the basic decision on whether to have a conscious policy of restraining production in the 1980s.
- (e) The Rate of Issue of New Licences. This is not discussed in the report but a policy line - rapid issue of licences - is asserted in Mr. Howell's covering paper. It is by no means self-evident that this is the best course. Control of the rate of issue of licences is the one "painless" instrument available for Government to influence the future course of oil output. Moreover it is one which can be exercised flexibly, e.g. by keeping successive licensing rounds reasonably small but varying the time intervals between them as circumstances - including the rate of actual discoveries of oil - require. This is a policy to which the last Government was feeling its way and consideration of it should not go by default.

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6. The Content of the Statement: this must obviously depend on the particular decisions reached by E Committee. It is however worth bearing in mind that, in an uncertain situation, there is little point in closing options until it is operationally necessary to do so. If nevertheless Ministers decide now that they want to forgo the benefits of the peak oil production period in the 1980s for the benefit of the 1990s there is a lot to be said for a fairly comprehensive statement so that the oil industry knows where it stands. If on the other hand Ministers do not want to follow this path, or do not want to decide now whether to follow it or not, any early statement probably needs to do little more than deal with gas flaring. The "Varley assurances" already inhibit the use of production cutbacks until 1982 and, while the oil industry would clearly like to know whether it faces such cutbacks - and probably needs to know in the course of 1981 - it is doubtful whether the Government needs to commit itself yet to foregoing this instrument.

7. Timing of the Statement: an early statement that we intended seriously to reduce oil production below what it would otherwise have been in the 1980s would be criticised in Europe and seized upon by OPEC as a justification for any production cutbacks they may wish to impose. Any major statement pointing in the direction of reduced production should therefore be deferred at least until the European Budget issue has been settled and probably until OPEC has made a move on its own to reduce the output of its member countries. A minor statement, e.g. confined to gas flaring, could however be made at any time, because its justification does not depend on depletion policy as such but rests on the avoidance of waste of high quality fuels.

HANDLING

8. You will want to ask the Secretary of State for Energy to introduce his paper and then seek contributions from the Chancellor of the Exchequer on the financial and balance of payments aspects and the Foreign and Commonwealth Secretary on the overseas aspects. Other Ministers, and Sir Kenneth Berrill, may then wish to join in.

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CONCLUSIONS

9. You will want to record specific conclusions on:-
- (a) The major issue of whether we should decide now to seek to avoid being a net exporter of oil in the 1980s.
 - (b) If so, whether colleagues are prepared to endorse the full range of actions listed in the report by officials and on the pace of issue of new licences.
 - (c) If not, whether to support the recommendation by officials for a "tight" approach to gas flaring.
 - (d) What should be said - depending on the answers to (a), (b) and (c) above.
 - (e) When any statement should be made: a statement confined to gas flaring can and should probably be made quickly; a statement announcing a much wider policy ought to be delayed and its actual timing subject to a specific decision involving both yourself and the Ministers most immediately concerned.

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Robert Armstrong

10th March 1980