

Original filed  
Energy July 19-7th Round  
licensing.

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PRIME MINISTER

7th ROUND OF LICENSING AND DEPLETION POLICY

(E(80) 31, E(80) 32 and a letter dated 27 March from the Secretary of State for Energy to the Foreign Secretary)

BACKGROUND

There are three issues -

- a. The size of the 7th Round (E(80) 31);
- b. Revenue from the 7th Round (E(80) 32);
- c. The timing of an approach to the oil companies about depletion policy (Mr Howell's letter of 27 March to the Foreign Secretary.)

2. Size of the Round: E decided last year that the 7th Round should comprise 70 blocks (E(79) 13th meeting). Mr Howell wants to be free to offer more blocks than this. His preferred method - paragraph 8 of his paper - would be to invite applications for 70 specified blocks and to allow the oil companies to bid for further blocks of their own choosing in the northern North Sea - with something like 20 to 40 blocks being handled in this way. This second proposal would no doubt be very welcome to the oil companies, but can be criticised on the grounds that it enables them to "pick the eyes" out of the remaining territory and thus diminish the attractiveness of future licensing rounds. Against this Mr Howell will argue that it is the quickest way to get extra production in the 1990s when North Sea output may be falling sharply. Colleagues will have to decide whether to accept Mr Howell's advice (reinforced by a late minute from the Foreign Secretary supporting a larger round for 'European' reasons). It will be important to distinguish between a larger round as such and a round enlarged by the choice route. The former may be easier to accept than the latter.

3. "Auctioning licences": Mr Howell wants to issue licences on the old discretionary basis as being, in his judgment, the best way of meeting our other objectives such as favouring smaller British companies. The Chancellor sees auctioning of at least part of the licences as a quick and easy way of raising a lot of money. No one knows how much could be raised this way but the very limited auctioning experiment in the 4th Round raised over £100 million and a

good deal more may be obtainable now. Auctioning is of course common practice in the United States of America. As a half-way house Mr Howell is now suggesting in his paper (E(80) 32) that more revenue could be raised by imposing higher licensing charges on at least some of the blocks, with discretion as to who gets the licences being left firmly in his hands. He estimates the possible receipts from this as perhaps £80-£100 million if the higher charges were confined to the 'own choice' blocks recommended in his other paper (E(80) 31).

4. Mr Howell is right in saying that auctioning limits his discretion, but there are two points to be made. First, it is by no means clear that Mr Howell's objectives are not obtainable within an auctioning system, especially if he follows the Chancellor's suggestion of auctioning some licences and allocating others. Indeed there may be other ways of solving the problem, eg applicants could be required to provide themselves with British or European partners. Second, the exercise of Government discretion in a situation where very large sums of money are at stake is an inherently uncomfortable operation. An auctioning system based on fair and known rules would be a major safeguard against charges of impropriety. There is of course absolutely no reason to suppose that such charges would have substance but the risk is there.

5. Consultation on depletion policy: At the meeting of E on 11 March (E(80) 9th Meeting, Item 1) when depletion policy was discussed, it was agreed that Mr Howell should defer discussion with the oil companies about depletion policy "until after the European Council meeting at the end of March". Now that the Council has been deferred Mr Howell wants to move straight away to such consultation while reserving any statement on policy until after the postponed Council is out of the way. The considerations which influenced the earlier decision, however, still stand and colleagues may feel that Mr Howell should curb his impatience for a further month. A late minute from the Foreign Secretary to Mr Howell has urged just this.

#### HANDLING

6. You may find it convenient to tackle the issue separately in the order set out above and to invite Mr Howell to introduce each in turn.

CONCLUSIONS

7. Subject to discussion, these might be:-

Either (i) to confirm the previous decision that the 7th Round should consist of 70 blocks,

Or (ii) to agree on a higher number (Mr Howell's original bid last year was for 100 blocks);

And (iii) to record a specific decision on whether the oil companies should be allowed to choose some of the blocks for themselves.

(iv) Either to agree that some of the licences should be auctioned with details to be settled between the Secretary of State for Energy and the Chancellor,

Or (v) to accept the Secretary of State for Energy's proposal for a higher charge for some blocks while retaining allocation by discretion.

(vi) To agree on whether Mr Howell should or should not enter into discussions with the oil companies on depletion policy before the next meeting of the European Council.

ROBERT ARMSTRONG

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