

Prime Minister to see

cc Mr. Wolfson
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PRIME MINISTER

GAS GATHERING IN THE NORTH SEA

I have seen Mr. Ibbs' note of 8 September. I should like to emphasise three wider political points arising out of the report by officials which Mr. Ibbs has presented.

Extension of Public Sector Monopoly Power

2. Whatever its advantages, the fundamental objection to proceeding with a public sector integrated line is that it would involve - certainly initially, and probably for some time - a major extension of public sector monopoly power:

(i) An important condition for the integrated line's operation is likely to be the banning of competitive private sector pipeline at least for the next decade.

(ii) The Government will feel that it has to use its depletion powers to improve the profitability of the line by controlling gas development throughout the North Sea in order to provide sufficient throughput e.g. by developing expensive Northern Basin gas ahead of cheaper Southern Basin gas. Perfectly legitimate private sector business decisions would be constrained for the sake of the publicly sponsored integrated line.

(iii) The BGC Chairman has stressed to the CPRS that BGC would not accept financial responsibility for the integrated line if their monopsony is removed. The Department of Energy hope to persuade the Corporation to drop their reservations. But as the CPRS note explains



BGC's wish to retain their monopsony is understandable if they are responsible for the integrated line.

(iv) By the 1990s some 20-25 per cent of UK gas supplies could be coming through the integrated line. At winter peak demand that amount of gas would not be easy to replace from elsewhere in BGC's system. The staff operating this line will thus have enormous industrial muscle. The multiple approach reduces this concentration of industrial power.

In short, a decision to proceed with a public sector integrated line would effectively reinforce BGC's monopsony, which it is our policy to remove and which is at the root of our difficulties in enlisting private sector support. We should have embarked on a public sector planning approach to gathering gas which is in sharp distinction to the very successful private sector solution adopted hitherto to bringing the North Sea oil ashore.

Risks and Rewards

3. In view of the private sector's unwillingness to risk their shareholders' money in financing an integrated line, there needs to be strong reasons before the Government commits public money, especially as:

(i) It is agreed that the private sector multiple pipeline system should enable the vast bulk of the £25 bn gas to be brought ashore, and is thus a very good economic prospect.

(ii) 100 per cent public sector financial support for the line does nothing to reduce the degree of financial exposure and risk which the private sector has found so unattractive. The main financial risk in investment in the integrated line is that there will be insufficient gas to go through the line in its early years; and this



is in the hands of the oil companies. Mr. Ibbs' note points out that firm gas developments current amount to 2.3tcf and the scheme needs an estimated 4tcf of gas to ensure its commercial viability.

Thus, the integrated line entails a very large commitment of public funds, and a commitment which is not free of risk. A decision to go that way (with its other attendant disadvantages) does not appear to be justified by the prospect of benefits over and above the benefits obtainable from the multiple scheme where the financial risks lie with the private sector. All our experience over recent years has emphasised the unwisdom of using public credit to support the financing of leviathan projects like the integrated line in conditions of great uncertainty where there is a private sector alternative available.

Public Expenditure and the PSBR

4. If it could have been demonstrated that there was an overriding case for the public sector integrated line, I would not have objected to it solely because of the need to keep down the public expenditure totals and the PSBR over the vital next few years of the Medium Term Financial Strategy - though any increase in respect of the pipeline would, if course, mean corresponding economy in other directions. But the necessity for the line is far from overwhelming. In these circumstances it is only prudent to husband the limited public expenditure resources which are available for programmes which cannot be undertaken, or effectively matched, by the private sector.

Presentation

5. The presentation of a decision not to proceed with the integrated line would, of course, need careful handling. A possible approach might be:

(i) Further discussion of gas gathering has convinced Ministers that the oil companies will bring the gas ashore. There is no need for a grandiose nationalised industry project financed from the peoples' pockets.



(ii) The highly successful development of the Northern Basin oil fields has been carried out largely by the private sector (with much of the planning being carried out when Mr. Benn was Secretary of State), with virtually no risk to public funds and enormous profit to the country. The Government intends to continue to back this record of success by letting the private sector develop the North Sea gas fields for the benefit of the country as a whole.

6. I am sending copies of this minute to the Secretary of State for Energy, Industry and Scotland and to Mr. Ibbs and Sir Robert Armstrong.

Jim Rutter

PP (G.H.)

9 September 1981

*Approved by the Chancellor and signed
in his absence.*