C O N F I D E N T I A L

Energy

PM

Mr Alexander

NBPM

[illegible]

1/5

01 211 6402

The Rt Hon Sir Ian Gilmour Bt MP
Lord Privy Seal
Foreign and Commonwealth
Office
Downing Street
London
SW1A 2AL

29th April 1980

Dear Ian

BNOC OIL PRICES

Thank you for your letter of 18th April.

As you know, HMG has no power to control the prices at which UKCS crude is traded. BNOC for its part has to pay the going market price to its supplying companies for the oil it acquires under the participation agreements, and in the event of any disagreement over prices there is provision for expert determination which is binding on both sides.

It is, of course, true that in recent months we have sought the co-operation of BNOC and producing companies on the timing of price adjustments, but we have to recognise that BNOC cannot withhold full market prices to their suppliers. Nor can we expect unreasonable delay in setting prices. Quite apart from the risk of challenge at expert determination, BNOC as the largest third party trader of UKCS oil has a limited time available under its contracts to fix its selling prices. It cannot therefore be expected to delay reaching agreement on its buying prices without inviting precisely the suggesting of compensation to which I referred in my letter of 14th April.

There is an inherent dilemma, as you point out, between on the one hand BNOC's need to move at the right moment in market terms and HMG's desire on the other from time to time to see UKCS price increases timed so as to minimise political repercussions. I had in fact been considering putting a note to colleagues reviewing the experience of recent months, and certainly agree with your suggestion that it would be useful for our officials to get together to examine the way current price determination works. I have accordingly asked my officials to put this in hand with other interested Departments.

I am copying this letter as before to the Prime Minister and the Chancellor of the Exchequer.

Yours ever

David

D A R Howell

CONFIDENTIAL

Energy

SECRETARY OF STATE FOR ENERGY
THAMES HOUSE SOUTH
MILLBANK LONDON SW1P 4QJ

01 211 6402

Rt Hon Sir Ian Gilmour Bt MP
The Lord Privy Seal
Foreign and Commonwealth Office
Downing Street
London SW1

29 April 1980

Dear Ian

BP/BNOC OIL SALES

Thank you for your letter of 14 April.

I asked my officials to get together with yours to see if a way could be found of recasting the side-letter from BP to provide better protection against any legal challenge, and was glad to learn that you are now able to accept the amended side-letter - a copy of which I attach - which has been agreed with BP.

I should perhaps add for the record that my references to clawback in our earlier exchanges did, of course, relate to the arrangements as a whole for dealing with a supply shortfall and not only termination. As you know, both BP and we think it unlikely in a sub-trigger situation that circumstances will arise in which the provision for termination would need to be exercised.

I am copying this letter and enclosure as before to the Prime Minister, the Chancellor of the Exchequer, other members of OD(E), the Attorney General and Sir Robert Armstrong.

Yours ever

David

D A R HOWELL

CONFIDENTIAL

POSSIBLE SIDE LETTER FROM BP TO SECRETARY OF STATE FOR ENERGY

You emphasised the importance attached by HMG to BP's role as a supplier of crude oil to markets in the European Community, and asked us to consider in this context the effects of the proposed new arrangements.

The arrangements comprise Sales Agreements with BNOC, which will provide us with an estimated additional supply of 39 million tons over the years 1980/82; and an Agreement dated X concerning the supply of oil to the UK during a supply shortfall, which we entered into in order to secure these additional supplies. It is our view that taken overall, these arrangements will increase the oil available to our Associate companies including those in the EC.

It is not possible to foresee the circumstances which may arise in future supply crises and what action we would take in circumstances where our obligation under the Agreement dated X were invoked. It would be our intention to seek to cover Group requirements through operational flexibility, including drawing from stock and/or additional purchases on the open market; and, given that the Agreement refers to a supply crisis sufficiently limited in extent as not to trigger the IEA/EEC emergency mechanisms, we would expect to be able to procure the additional supplies involved without reducing the volume of supplies to our Associate companies.

This letter shall be accorded the same degree of confidentiality as the Agreement to which it relates.

CONFIDENTIAL

LORD PRIVY SEAL

Energy

Foreign and Commonwealth Office
London SW1

18 April 1980

CF. we certainly received this

Dear David,

BNOC OIL PRICES

Thank you for your letter of 14 April. The price adjustments have now been made and I hope that they will not in the event give rise to difficulties. My purpose in writing now is to urge that we establish procedures to ensure that BNOC should not in future so act as to pre-empt proper Ministerial discussion of proposed price increases.

As I understand it, the whole basis of our consideration of BNOC's pricing policy last November and last January was that you had considerable scope for influencing BNOC's decisions. Indeed, your minute of 3 January to the Prime Minister sought agreement to authorise BNOC to follow a particular course. The increases then involved were greater, but the political situation just before the European Council is at least as delicate. I do not accept that BNOC should be the sole judge of what lies within their commercial competence in such circumstances.

I am still more concerned at the implications in your letter that BNOC got themselves into a position where they would not only lose money if they did not put up their selling price but considered themselves entitled to claim compensation from HMG. If they are able to proceed in such a manner, it will be an extremely important factor in any future collective Ministerial consideration of

/BNOC's

The Rt Hon David Howell Esq MP
Secretary of State for Energy
Thames House South, Millbank SW1

BNOC's pricing policy, and I should like to have a much clearer idea of what may be involved.

A useful first step might be for officials of the interested departments to consider the implications of what happened on this occasion in the light of the concerns I have expressed. It would be helpful if one of your people were to call a meeting for this purpose. I am no more anxious than you for the Government to become involved in the minutiae of BNOC's commercial activities, but pricing decisions will remain politically sensitive in the international arena and it is important that decisions should not be thrust upon us by the Corporation.

I am copying this letter to the Prime Minister and the Chancellor of the Exchequer.

Yours ever

Ian

CONFIDENTIAL

Energy

SECRETARY OF STATE FOR ENERGY
THAMES HOUSE SOUTH
MILLBANK LONDON SW1P 4QJ

01 211 6402

NBPM
MS

The Rt Hon Sir Ian Gilmour Bt MP
Lord Privy Seal
Downing Street
London
SW1A 2AL

14 April 1980

Dear Ian

BNOC OIL PRICES

Your Private Secretary wrote to mine today commenting on my Private Secretary's letter to the Private Secretary to the Prime Minister of the 11th April reporting the small price adjustments BNOC is about to make.

BNOC do not require my authority to make these changes, which are within their commercial competence. They have said today that they are not able further to defer action with their customers without incurring losses on the differential between their buying price (which is not ultimately theirs to determine) and their selling price. To defer action tomorrow, they would require an undertaking of compensation by HMG. In any case, I cannot accept that anxiety about inappropriate comparisons between North Sea prices and Algeria's nominal price, rather than its actual price, should determine the price for North Sea oil. I regret, therefore, that I cannot accede to your request to intervene with the Corporation.

I am sending a copy of this letter to the Prime Minister and to the Chancellor of the Exchequer.

Yours ever

David

D A R HOWELL

15 APR 1980

N BPM
MJ

Energy

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

15th April, 1980

T. Lankester, Esq.,
Private Secretary,
10, Downing Street,
LONDON,
S.W.1.

Dear Tim,

UKCS CRUDE OIL PRICES

The Chancellor of the Exchequer has seen the letter of 11th April from Denis Walker in the Secretary of State for Energy's office about BNOC's proposal to hold the increase in Forties crude to around 50c and to propose changes to other qualities of UKCS crudes ranging from zero for flotta to about 65c for the highest qualities.

The Chancellor does not dissent from the approach set out in the Secretary of State's letter.

I am sending copies of this letter to George Walden, Denis Walker and David Wright.

Yours

John

A.J. WIGGINS

15 APR 1980

COMMERCIAL - IN CONFIDENCE

HS

cc HMT
FCO
CO

Energy

14 April 1980

UKCS Crude Oil Prices

The Prime Minister has seen your letter to Tim Lankester of 11 April. She is content, subject to the views of colleagues, that your Secretary of State should act as suggested in your letter.

I am copying this letter to John Wiggins (H.M. Treasury), Paul Lever (Foreign and Commonwealth Office) and David Wright (Cabinet Office).

N.J. SANDERS

Denis Walker, Esq.,
Department of Energy.

TL

Prime Minister

Agree subject to colleagues' views?

11/4

Yes no.

SECRETARY OF STATE FOR ENERGY
THAMES HOUSE SOUTH
MILLBANK LONDON SW1P 4QJ

01 211 6402

Tim Lankester Esq
Private Secretary to the
Prime Minister
No 10 Downing Street
LONDON SW1

11 April 1980

Dear Tim,

UKCS CRUDE OIL PRICES

The Prime Minister will wish to know of some small impending adjustments in the price of UKCS oil.

Over the last two weeks of March, BNOC sought the agreement of their suppliers under participation agreements to the continuation into the Second Quarter of the prices for UKCS oil which applied during February and March. You will recall that during January BNOC had held the price of Forties crude to \$29.75 per barrel (which was below the price of \$29.97 per barrel for Nigerian Bonny light - then the most moderately priced comparable African crude), making a \$4 increase to a price of \$33.75 in February after the Nigerians increased their prices by \$4.21. The spread of prices is illustrated on the attached table.

BNOC encountered some supplier opposition to this proposal for Second Quarter prices, on the grounds that the 21 cents foregone in February should be made up. Further to this, BNOC informed the Secretary of State before Easter that the Nigerians had made a further price adjustment of 51 cents in their official selling price from the 1st April, bringing the official price for Bonny light to \$34.69 per barrel, and that this would make it necessary for the Corporation to concede some related adjustments in its buying prices for the current quarter. The Secretary of State told the Corporation that the market should be left to determine the appropriate current valuation for UKCS crude, but that it would be helpful to HMG if the timing of any change could be deferred for a week or two. He had in mind particularly the concerted efforts being made to deny the Iranians their \$2.50 proposed price increase.

BNOC agreed to this request and confined their action before Easter to reserving their position on selling prices with those of their customers due to take deliveries over the next few days. They have today informed the Secretary of State that it is the Corporation's formal judgment that

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these price adjustments must be offered to their suppliers and customers, in exercise of the Corporation's commercial responsibility and that they will act to this effect on Monday. They believe they can hold the Forties price increase to around 50 cents and will propose changes to other qualities of UKCS crude ranging from zero for Flotta to about 65 cents for the highest quality crudes in an attempt to reflect more appropriately the quality differentials between the various crude types.

The Algerians have not yet announced an increase comparable to that imposed by Nigeria, though they have told the Corporation that they will make a related change (which the Corporation expect to be arbitrarily back-dated to the 1st April) and their official price in any case already embodies a $3 "exploration premium" which takes it well ahead of UKCS prices. There has been no word of a further price change from Libya, but the latest Nigerian move in fact does no more than bring the Nigerians and Libyans into line. This series of modest price adjustments would in fact represent a move towards more appropriate market relativities between the African crudes and between them and UKCS crudes.

The Secretary of State is of course very conscious of the need to seek to avoid any change which could prejudice the action being taken to resist the Iranian price increase. That increase however is of an entirely different order and is clearly a political attempt to ratchet up the oil price rather than the sort of market adjustment represented by these modest changes. We have consistently held to the doctrine that the market must ultimately determine the levels of UKCS prices - indeed, as a purchaser, BNOC has no means of imposing a price below the market. Moreover, it is in the interests of restoring order to the market that prices should be set at latest in the first few days of a quarter and not retrospectively. Though we attach importance to UKCS prices being seen to follow and not lead world prices for comparable crudes, it is clearly defensible to move to follow the Nigerians when the Libyan and Algerian official prices (leaving aside additional premia charged in many cases) are already ahead of the others. In these circumstances, my Secretary of State is not disposed to seek to overrule the Corporation's commercial judgment on the handling of these small proposed adjustments.

I am sending copies of this letter to the Private Secretaries to the Chancellor, the Foreign Secretary and to Sir Robert Armstrong.

Yours ever,

Denis

Denis Walker
Private Secretary

SEQUENCE OF PRICE INCREASES

($/b)

Country	Libya	Nigeria	Algerian	UK
Crude	Es Sider	Bonny Light	Saharan Blend	Forties
Mid Dec.	29.78	29.97	30.00	26.02
1 Jan 80	34.50	29.97	30.00 (+3.00)*	29.75
4 Feb 80	34.50	34.18	34.21 (+3.00)*	33.75
1 Apl 80	34.50	34.69	34.21 (+3.00)*	34.20

*Compulsory "Exploration" surcharge.

11 APR 1980