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19 October 1981

CABINET

MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

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GAS LEGISLATION
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Memorandum by the Secretary of State for Energy

Introduction

1. Cabinet agreed on 24 September (CC(81)32nd, Minute 5) that powers should be taken in the 1981/82 Parliamentary Session to direct British Gas Corporation (BGC) to dispose of specified interests and to abolish their gas purchase monopsony. The purpose of this memorandum is to describe my proposals in more detail in order that preparation of legislation can proceed. I have agreed with the Lord President of the Council that it would be convenient to make these additional provisions by expanding the Petroleum and Continental Shelf Bill for which I already have policy approval.

Disposal of Assets

2. My present powers under the Gas Act 1972 to direct BGC to cease activities and dispose of assets can only be used when I am satisfied that I will not thereby impede the proper discharge of the Corporation's duties. Moreover they do not enable me to require the Corporation to pass the proceeds of the sale of assets to the Government. These powers are not therefore sufficiently wide for the purposes for which we shall wish to use them (eg disposal of offshore oil assets and later, showrooms).

3. I propose therefore to seek wider powers of direction. The new powers would enable me to direct the Corporation not only to cease activities and to dispose of certain assets wholly or in part but also, where necessary, to arrange that particular assets are held by a subsidiary of which shares would then be offered to the public. I propose to use these powers in the first instance to privatise BGC's offshore oil assets. In such cases, I might also wish to direct that share schemes should be available in which the Corporation's employees could participate. In all cases of disposal, I would wish to have the power to claw back the proceeds of sale for the Exchequer.

The BGC Monopsony/Monopoly

4. My proposal is that the forthcoming legislation should eliminate BGC's gas purchasing monopsony and break their monopoly over sales to industrial and possibly larger commercial consumers. It was this monopsony/monopoly which, *inter alia*, made it ^{important} to get a private sector gas-gathering pipeline off the ground. The ^{good} ~~best~~ intention would be to enable these consumers to purchase gas without BGC acting as intermediary. The

monopoly of gas supply to other (including domestic) consumers would however be preserved because in this case the existence of a monopoly supplier confers genuine advantages (security of supply, safety and lower costs from economies of sale): in short, the classical argument for a public utility. The detailed changes which I propose are set out in Annex A, which also describes the rights and duties of BGC which support the present monopsony/monopoly position. In framing my proposals, I have assumed, on the basis of legal advice, that there will be no case for compensating private landowners when third party gas is transmitted through existing pipelines under their land. If we do encounter problems on this, I will consult my colleagues further.

5. There are two other matters to which I should draw the attention of colleagues. The first of these is the landing requirement for gas, which could come under greater attack if in due course some companies seek approval to export gas and we are unwilling for this to happen. The second is the need to ensure that BGC's transmission system can be used as a common carrier by the private sector on ~~firm~~ ^{fair} and reasonable terms, so providing effective competition in the gas market. This will require regulation which will have staffing consequences.

6. A note on both these points is at Annex B. Any additional risk of challenge to the landing requirement and the staffing consequences of having to regulate access to the BGC transmission are in my view far outweighed by the advantages which will flow from the changes I propose viz:-

- (a) an improvement in the efficiency of BGC, through increased competition;
- (b) an increase in gas exploration and production;
- (c) a better deal for the industrial gas consumer.

Recommendation

7. I seek my colleagues agreement to my detailed proposals as set out above.

Department of Energy

19 October 1981

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ANNEX A

PRESENT RIGHTS AND DUTIES OF BGC AND PROPOSED CHANGES

Present Position

1. The legal powers which have created BGC's monopoly position have derived over the years from the concept that a single public utility should operate the British gas supply system. The powers which create the monopoly position are paralleled by duties imposed on the Corporation. Section 52 of the Gas Act 1948 effectively gave Area Boards the sole right of supply of gas through pipes. Section 9 of the Continental Shelf Act 1964 removed that provision for offshore natural gas but required ministerial consent to the supply of such gas through pipes. Such consent could not be given for non-industrial purposes nor for industrial fuel purposes unless the relevant Area Board (subsequently BGC) had been given an opportunity of purchasing the gas at a reasonable price. Such consent had to be given for supplies for industrial non-fuel purposes. Sections 8 to 11 of the Energy Act 1976 repealed section 9 of the 1964 Act replacing it with similar (but more elaborate) provisions. There have so far been no formal approaches by producers to the Secretary of State to seek his decision on whether, for the purposes of these provisions, they have offered gas at a reasonable price.

2. These privileges may be seen as the converse of BGC's duty under the 1972 Act

"to develop and maintain an efficient, co-ordinated and economical system of gas supply for Great Britain, and to satisfy, so far as it is economical to do so, all reasonable demands for gas in Great Britain".

Alongside this general duty, BGC are obliged to supply gas on request to any premises within 25 yards of an existing main, subject to the limitation that they need not supply any premises with more than 25,000 therms a year (a small amount by industrial standards). This last limitation was introduced by section 13 of the Energy Act 1976 and strengthened by the Gas Act 1980.

Proposed Changes

ANNEX A

A. Gas purchase/supply3. i. Repeal of sections 8(3) and 9(3) of the Energy Act 1972

This will remove the need for BGC to have first option on purchase of UKGS gas at a reasonable price before any person can supply it, or a purchaser can use it for industrial purposes. This will put supplies or use of such gas on the same footing as supplies of gas for non-fuel industrial purposes over which BGC enjoys no special rights of first refusal.

ii. Amendment of section 29 of the Gas Act 1972

This section will need to be amended to put the supply of manufactured and imported gas on the same basis as UKGS gas as in i above.

iii. Consequential amendments to other sections of the Gas Act 1972

Sections 26 and 31 deal with standards of quality, pressure of gas supplied, and gas safety, but only apply to BGC as gas supplier. The provisions will need to be extended to all potential suppliers. Section 25 dealing with methods of charge and tariffs will also require amendment. Some other minor consequential amendments will be needed to other sections.

iv. Amendment of section 4 of the Petroleum (Production) Act 1934

This gives BGC first offer rights at a "reasonable price" on gas found onshore in Britain. This will be abolished.

v. Amendments may also be needed consequential to i-iv above to prevent anomalies in relation to the Gas Act 1972. This is being studied further.

2.

ANNEX A

B. Gas transmission/distribution

Powers will be vested in the Secretary of State for Energy to regulate common carrier questions. An additional duty on BGC not unreasonably to refuse to carry private sector gas may be needed. Sections 26 and 29 to 31 of the Gas Act 1972 will need to be modified to take account of the impact of the changes on the Secretary of State's responsibility for safety and quality standards. Where BGC transmit gas under sole rights granted by landowners, in respect of pipelines under their land, such rights will require modification.

BREAKING THE BGC MONOPSONY/MONOPOLY:
SOME CONSEQUENTIAL EFFECTS.

The Landing Requirement

1. The requirement that gas from our Continental Shelf must be landed in the UK is already vulnerable to attack on grounds that it is incompatible with the Treaty of Rome. Removal of the BGC monopsony is not directly connected with the landing requirement since the monopsony only applies to gas coming ashore in the UK. But this step could possibly encourage some licensees to seek approval to export gas. We would have to consider the desirability of this when the time came and, if we decided against, I have available powers which might indirectly be used to prevent gas from being exported. Nevertheless an important case, or a succession of other cases, in which I used these powers might lead to our being challenged under the Treaty.

BGC Pipeline System

2. An important problem in achieving the objectives of the Bill stems from the difficulty which private sector suppliers may have in transmitting gas to the point of consumption. I intend that the private sector should have greater freedom under the new regime to build its own onshore gas pipelines, but in practice it may only be economic to do so in the case of large bulk supplies or supplies to customers whose premises are near the landing point of the gas. To encourage private sector deals on any scale it will be essential for access to be given to the national transmission system operated by BGC. As a first step it will probably be necessary to impose a duty on BGC not unreasonably to refuse to carry private sector gas. But that will not be enough in itself. Difficulties are still likely to be encountered if BGC act, or are alleged to act, unreasonably (for example by proposing unfair charges for transmitting gas or claiming to have insufficient capacity).

3. A form of regulation will be needed to overcome these problems and I propose that appropriate regulatory powers should be vested

in me. This will however have staffing consequences for my Department.

Financial and Staffing Consequences

4. I shall need initially 8 to 10 staff, including professional grades, to deal with the relatively small number of cases which might arise in the early stages of the regulation process. Some of these staff will be required before the legislation is passed to prepare the groundwork. I might also need to employ one or two consultants to help with this in the first year. If the policy succeeds in due course in generating a great deal of direct business between private sector producers and consumers, staff requirements could rise to perhaps 40 to 50. If that stage were reached we would have to consider transferring the work to a separate regulatory agency. While the number of staff required for this work remained in single figures, I would propose to take them from within current staff ceilings. Beyond that stage the staff requirements for this task would have to be additional to my staff ceilings. Significant financial consequences, apart from those arising from staffing and the employment of consultants outlined above, are not anticipated.