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CABINET  
MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

BNOC: PRIVATE SECTOR PARTICIPATION

MEMORANDUM BY THE SECRETARY OF STATE FOR ENERGY

Following the meeting of the Committee on 12 December 1979 (E(79)19th Meeting), there have been further discussions under the Prime Minister's chairmanship concerning my proposals for private sector participation in BNOC - which were set out in E(79)67. In these discussions it was decided that:-

- (i) my proposals for separating BNOC into distinct trading and operating arms should be adopted;
- (ii) that our ultimate objective should be to sell shares in the operating arm to the general public;
- (iii) the necessary legislation should be drafted accordingly;
- (iv) further consideration should be given to the timing, speed and extent of disposal of such shares.

2. This paper sets out my recommendations reached in consultation with the Chancellor of the Exchequer on the timing of legislation; on an early announcement of our policy for BNOC; on the timing and extent of share sales; and on the question of the extent to which BNOC (Trading) should have options over BNOC (Operating)'s oil.

Timing of the legislation

3. We have announced our intention to legislate this session but in the light of my discussions with the Chancellor I now think it would be unwise to push ahead this fast; our reasons for this are:-

- (i) Work is proceeding on drafting but even on the most optimistic timetable we could not expect to achieve the Bill without an extremely compressed Committee Stage, and probably with a need for a substantial spill-over after the recess.
- (ii) The Chancellor has recently raised two points on my original proposals which must be resolved before we can proceed further

with drafting the legislation (para. 9 refers).

- (iii) We have not yet decided on the timing of share sales, and the Chancellor is not relying on receipts for the 1980/81 PSBR. Even if we got the legislation through this would not assure us of receipts in 1980/81, since the administrative work involved in transferring all the assets to BNOC (Operating), and preparing for the sale will be complicated and take time.
- (iv) I have had the Chairman of BNOC's views on both our proposals and the timetable. Predictably he questions the desirability of the basic political objective of splitting the trading and operating sides and the viability of the Trading side as a separate entity. But he also emphasises his concern that the transfer of assets etc. to the new company will be complex. While legislation is not needed to deal with all the problems that arise I agree with him that our legislation must be compatible with this operation. If we push it through this session, we may not be able to give these issues the detailed consideration which is essential. Mr. Utiger does not think that postponement of the legislation would give rise to insurmountable management difficulties in BNOC, although we would need to appoint a new Chairman prior to the publication of the legislation.

I have therefore reluctantly come to the view that we should plan the introduction as early as possible in the Autumn. The Chancellor agrees with this.

#### Timing of a further announcement

4. We will need to present this decision in the right light in the light of our earlier announced intention to bring forward legislation this session. An announcement within the next fortnight is desirable but it will soon become clear anyway that legislation of this controversial nature is not now feasible this session. This change of plan is likely to be greeted critically by some of our supporters but I think this can be handled provided I have the full backing of my colleagues in terms of our broad political strategy and that its announcement is coupled with a clear statement of our intentions for BNOC.

#### Timing, speed and extent of share sales

5. It has been implicit in all our discussions that the two arms of BNOC (Trading and Operating) should be quite distinct, with separate managements; and that the Operating company should be in the same position as other private sector oil companies operating in the North Sea. The reasons for this approach are:-

- (a) to establish BNOC (Operating) as a truly independent British company competing on equal terms with the oil majors; a second BP as it were;
- (b) to offer a channel for private sector investment free from risk of Government interference;
- (c) to separate the highly political Trading operation from the commercially oriented Operating side.

Such a reclassification to the private sector will benefit the PSBR with the proceeds of sale of shares but will lose to the PSBR the benefit of the expected subsequent positive cash flows of BNOC (Operating) other than the dividend on the residual public sector stake.

6. The essential element of our policy to put over is that BNOC (Operating) is to be completely independent of BNOC (Trading) and of Government interference or control. This is needed to make clear our fundamental approach to privatisation and to ensure successful flotation of the shares. Our merchant bank advice is that this calls for a clear statement of intent on the part of the Government to reduce the public sector stake to minority status. I therefore believe that we must make clear when we announce the deferral of the legislation that our ultimate intention is to dispose of a majority of the shares in BNOC (Operating). This will underline our commitment to its independence, but does not commit us prematurely to any prescribed timetable for sale of shares. If we cannot be plain on this point we expose ourselves to charges of indecision which will certainly be exploited by the Opposition, putting us on the defensive in an area where we should be scoring positive political gain.

Oil options

7. I have given further consideration to this in the light of the discussion of the Committee on 12 December 1979. My conclusion is that BNOC (Trading)'s option on BNOC (Operating)'s oil should be the normal 51% because:-

- (a) this will emphasise that BNOC (Operating) is to be treated on the same footing as other independent oil companies; any other arrangement would call into question whether we really intended to create a proper independent operation. Our merchant bank advice is that this is desirable to achieve the best possible price for the companies shares.
- (b) A special arrangement of 100% could lead to challenge in the EEC on the grounds of abuse of dominant position.
- (c) If BNOC (Operating)'s obligations to sell oil to the public sector exceeded the normal 51% applying to private sector companies, then it would be very difficult to argue that it was independent of the Public Sector, and I understand, it would also be difficult to classify it to the Private Sector and to count the proceeds of the sale as a PSBR reduction.

8. A draft statement covering the above points is at Annex. I propose to make it through a written Parliamentary Answer.

Outstanding points

9. There are two outstanding points that must be resolved before we can proceed further with preparing the legislation:-

- (i) Whether HMG or BNOC (Trading) should hold the residual public sector stake in BNOC (Operating);
- (ii) Whether the legislative provisions dealing with the powers of the new BNOC (Trading) should be more restrictively drawn than we had so far contemplated.

However these points are not essential to the proposed statement, and I will be reporting separately on them in the light of further discussion.

session with the Chancellor.

Recommendations

10. I seek my colleagues agreement to:-

- (i) deferring legislation until the earliest opportunity next session;
- (ii) stating clearly now that our intention is to separate the trading and operating arms of BNOC, putting BNOC (Operating) into the private sector and to be ready ultimately to reduce the public sector stake to a minority.
- (iii) BNOC (Trading)'s options over BNOC (Operating)'s oil being 51%, the normal participation arrangement.
- (iv) announcing these decisions within the next 2 weeks along the lines of the statement at Annex.

Department of Energy  
5 March 1980.

Q. "TO ASK THE SECRETARY OF STATE FOR ENERGY WHAT PLANS HE HAS FOR THE FUTURE OF THE BRITISH NATIONAL OIL CORPORATION?"

- A. I will be introducing legislation as soon as Parliamentary time permits in the new session to allow for the setting up of a company through which the British public will be able to invest in BNOC's offshore operations.
2. BNOC has two distinct functions. First its access to oil through the participation and royalty in kind arrangements gives it an important role as a large scale oil trader. In this role BNOC can play an important part in protecting vital national interests including security of supply and in providing oil supplies for our international partners in the EEC and IEA. We intend that this role should continue.
  3. Second, BNOC is an oil producing company working alongside other oil companies in the North Sea. We see no need to retain these operations within the State sector and we shall therefore give the public the chance to participate directly in BNOC's oil producing business.
  4. We have therefore decided that BNOC should be re-organised. The existing Corporation will concentrate on oil trading. The participation agreements which give BNOC options to take oil will be retained, and I will continue to call upon BNOC to dispose of royalty oil on my behalf.
  5. The exploration and production assets and operations will be vested in a new Companies Act company. We intend that this company will operate independently of Government and of BNOC, except to the extent that its UKCS oil will be subject to purchase options by BNOC under normal participation arrangements. We propose to make a substantial shareholding in the company available for issue to the general public. The Government will not seek to control the company through the residual public sector holding of the shares - which it is intended will ultimately be reduced to a minority.

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- 6. The Government wishes to see a wide spread of ownership and will ensure that in the allocation of shares full regard is given to the position of small investors and employees.
- 7. Implementation of these proposals will call for a major corporate re-organisation and for the transfer of contractual and other interests. This is bound to take time. But preparatory work on this and on the necessary legislation is underway. The timing of the share issue will be a matter for further consideration.
- 8. These proposals will result in a proper separation of BNOC's two functions of oil production and of oil trading. We will thereby provide a secure foundation for further development of the United Kingdom Continental Shelf in the national interest.

Department of Energy  
6 March 1980

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