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CABINET

MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY
SUB-COMMITTEE ON DISPOSAL OF PUBLIC SECTOR ASSETS.

DISPOSAL OF ENOC'S ASSETS TO BP :

NOTE BY THE SECRETARY OF STATE FOR ENERGY.

This paper examines the feasibility and implications of disposing all of ENOC's assets to BP. Consideration is divided between the major policy implications, the legal problems and the practical implications.

Policy Implications

2. As my paper on State involvement in the Oil Industry (ref. E(DL)(79)6) makes clear I attach the greatest importance to direct Government access to, and control over, the disposal of UKCS oil as a means of ensuring our security of supply. I foresee this being achieved mainly through the exercise of participation options, although also through the taking of royalty in kind. And I see it as essential that whatever agency disposes of this oil must be directly responsive to Government wishes.
3. If this oil were vested with BP as a result of BP taking over all of ENOC's assets, then the Government's control over it would be lost since Government intervention in BP's affairs can only be severely limited. Any change in the established relationship between the Government and BP designed to allow the Government to use BP as a direct instrument of disposal policy with regard to this oil could probably only be achieved by the Government acquiring the private sector shareholding of BP; but even if this proved avoidable, such a change in the relationship would have the effect of undermining BP's entire standing as a worldwide independent oil company, and would diminish the attractiveness of any offer to the public of BP shares.

4. The only realistic possibility therefore is to consider the sale of ENOC's upstream estate. Immediate sale, implying immediate breakup of ENOC, leaving a state oil trading organisation in Government hands, would:

- a) remove ENOC's equity oil from the Government's influence forthwith; it might be possible to secure option rights for the state oil trading organisation over at least 51% of the oil, but this would undoubtedly reduce the attraction of the package to BP.
- b) create immediate and considerable upheaval and uncertainty in the North Sea which a less precipitate approach would avoid.
- c) go against the long term aim, described in the main paper, of bringing private capital into State industries. (BP is seen as a multi-national major. ENOC's upstream interests would become a relatively small part of BP's overall interests, and would not provide the potential UK investor with the direct and undiluted involvement in a UK operation which would be provided by the formation of a ENOC upstream subsidiary or associate).
- d) create a gap - at a critical moment - in the Government's links with North Sea operations.
- e) give BP a vastly preponderant role in the North Sea.
- f) be a bad bargain for the tax payer since BP would be the sole buyer.

Legal Problems

5. Even if the policy difficulties outlined above can be overcome, there are a number of legal difficulties:

- i) ENOC's participation interests cannot be assigned without the consent of the other party to each agreement, and nearly all of the agreements specifically restrict assignment to another State Corporation (or a wholly owned subsidiary of one). Indeed having been made for the express purpose of enlarging the public sector interest, the companies could scarcely be expected to agree to "participation" by BP. The statutory framework for participation, including PSPA and Participation

Agreements Act 1978 would moreover need to be amended before any such result could be secured.

- ii) Co-licences in general have rights to first refusal of assignments of licence interests. The means of disposal to BP of all ENOC's licence interests would have to be so devised as to get round this difficulty.
- iii) BP would run the risk of a Monopolies Commission reference or other action under restrictive trade practices legislation, action by the EEC Commission under articles 85 and 86 of the EEC Treaty, and of anti-trust action in the US.
- iv) Legislation would be needed, as it would be for any substantial disposal of ENOC's UKCS interests.

Practical Implications

6. There are a number of practical implications that would need to be considered:

- i) BP should be able to finance the acquisition of ENOC's assets, either overseas or in the UK. But the likely sums involved could strain BP's financing facilities and might lead to diversion of planned investment elsewhere.
- ii) BP might be reluctant to take on all of ENOC's interest in 5th and 6th round licences, since these cover nearly all the territory covered by the two rounds, and would involve BP in disproportionately high exploration expenditure. Indeed the private sector holders of 5th and 6th round licences would not look kindly on BP acquiring all ENOC's interests in these rounds, since it would amount to a fundamental change in the basis on which licences had been applied for. Some disengagement from these interests would probably be necessary as a preliminary to disposal to BP.
- iii) BP's status as an international commercial organisation, independent of the British Government - which has been regarded as an important feature particularly for its US operations - could be called into question if it seemed that the UK Government was effectively transferring the Government stake in the UKCS to BP.

- iv) BP might well be able to take advantage of the unutilised Corporation Tax allowances in ENOC to offset its own Corporation Tax liability. While this might encourage BP to offer rather more for the interests, it would probably be to the net disadvantage of HMG.

Assessment

7. The foregoing points strongly suggest that we should rule out transfer to BP of ENOC rights to oil, unless we are willing to relinquish the security of supply that control over that oil ensures. The disadvantages and difficulties of transferring ENOC's entire upstream interests to BP are also numerous and in my view overwhelming. But if disposals are in contemplation, then BP is clearly a front runner - although probably not for the bulk of the 5th and 6th round interests. And there is no particular advantage in confining the field for disposal of these interests to BP, especially in view of the strong negotiating position this would put BP in. Moreover BP's interest in the upstream operations would be reduced if we retained a right for the State oil trading operation to acquire at market prices at least 51% of oil arising from the upstream stakes disposed of as I believe we should in the interests of security of supply.

Conclusions

- 8 (a) Outright disposal of all ENOC's assets to BP is not desirable or practicable.
- (b) The extent to which outright disposals of ENOC's upstream interests should be sought is a question that should be resolved by reference to the future role envisaged for ENOC - which is dealt with in my paper (ref E(DL)(79)6).
- (c) If, in the light of colleagues' consideration of that paper, it is concluded that purchasers for all or part of ENOC's upstream assets should be sought, then BP is a potential purchaser, but there is no advantage in looking exclusively to BP and indeed there may be disadvantages in terms of the sums realised.

D.A.R.H.

Secretary of State for Energy,

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