The Privatization

of

UK Oil Assets 1977-87:

Rational Policy-Making, International Changes

and

Domestic Constraints

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Abstract

Why did British politicians initiate, and why did civil servants facilitate, the complete disposal of the government's oil assets, a vital national resource? Public choice theory has traditionally found it difficult to explain the retreat of the state, not because the theory is flawed, but because insufficient attention has been given to the parameters that actors face at both the domestic and international level. Four sets of parameters are particularly relevant to this case: international, industry, bureaucratic and political, which I review in sequence.

First, though international factors are rarely incorporated into domestic policy-making analyses, they do have an impact. Realists' issue-specific models can be adapted to these analyses and help explain why Britain was forced to bow to international financial pressures and to work within the international oil structure. A balance of payments crisis in 1976 forced Britain's first asset sale while the development of a free market for oil (not dominated by a monopoly or cartel) made further sales more feasible, but not inevitable.

Second, state-owned companies were often obstacles to privatization. A closer examination of the companies' structures explains the differing reactions of the managers of British National Oil Company (BNOC), British Gas Corporation (BGC) and British Petroleum (BP) and their abilities to achieve their preferences. The management of BP favoured privatization while the managers of BNOC and BGC opposed the sales of their oil assets. Though they could not prevent the fulfilment of the government's plans, they were able to cause delays and affect the form which privatization took.

Third, contrary to budget-maximizing models, the British civil servants did not impede privatization. As members of a generalist bureaucracy, they were more concerned with their immediate work tasks and future career prospects across the civil service as a whole, than the long term future of the division or department where they were immediately located. In addition, because the Department of Energy was a relatively weak agency, individual level and career-maximizing strategies predominated rather than collective action strategies.

Finally, because political demands for privatization were weak, other supply-side factors dominated politicians' decision to select privatization. These included party political pressures to cut public spending by means of asset sales and personal political advantage, which encouraged policy entrepreneurs to bear the initial costs of a potentially hazardous innovation.

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Table of Contents

Abbreviations

AOPEC - Arab Organization of Petroleum Exporting Countries

b/d - barrels per day

BGC - British Gas Corporation

BNOC - British National Oil Company

BP - British Petroleum

CBI - Confederation of British Industry

CPRS - Central Policy Review Staff

DEn - Department of Energy

EC - European Community

EMS - European Monetary System

GDP - Gross Domestic Product

GNP - Gross National Product

IEA - International Energy Agency

MMC - Monopolies and Mergers Commission

MP - Member of Parliament

NCB - National Coal Board

OECD - Organization of Economic Cooperation and Development

OPEC - Organization of Petroleum Exporting Countries

PAC - Public Accounts Committee of the House of Commons

PM - Prime Minister

PSBR - Public Sector Borrowing Requirement

TUC - Trades Union Congress

US - United States

UKCS - United Kingdom Continental Shelf

List of Figures and Tables

Figures

Tables

Chapter One: Introduction

Privatization in Britain has been heralded by British politicians, the press and political observers alike as a radical break in government policy - not only for the British government, but for any government. Yet the sale of Britain's oil assets, vital resources in an oil dependent world, passed without much opposition or even much notice. The assets, Britoil, Enterprise Oil and Wytch Farm, and a majority shareholding in British Petroleum, were sold within a 10 year period, 1977 to 1987, reversing a policy which had lasted 73 years. In this dissertation I seek to explain why the government pursued this seemingly irrational policy and why there was so little opposition. This first chapter establishes the theoretical argument and approach. I first review the realists' understanding of state power and the control of natural resources, and then examine previous attempts to explain the retrenchment of government. Building on these insights, I present an alternative approach. Next, I review the methodology and finally outline the rest of the dissertation.

1.1. State Power and Natural Resources

Ever since Thucydides wrote *The History of the Peloponnesian War*, scholars have asserted that states seek to maximize their power and that natural resources are an essential component of that power.[1] Modern political realists have added evidence and analysis to support this view. The three main points of realism are that the state

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[1] Robert Gilpin, 'The Richness of the Tradition of Political Realism,' in Robert Keohane, ed., *Neorealism and its Critics* (New York: Columbia University Press, 1986), pp.308-9; and E.H. Carr, *The Twenty Years' Crisis, 1919-1939: An Introduction to the Study of International Relations*, Second Edition (New York: Harper and Row, 1964), pp.114-29.

is the key unit of analysis, that states seek power, and that states behave rationally.[2] Realists and neo-realists contend that states try to enhance the power and material well-being of their inhabitants and therefore, as Stephen Krasner asserts, 'states want power and control as much as wealth.'[3] One of the primary means to power is control of material resources. Robert Keohane, in his seminal work *After Hegemony*, argues that power is based on the control of material resources; similarly, G. John Ikenberry and Charles A. Kupchan assert: 'Power is directly related to the command of material resources.'[4]

Of all a state's resources, most scholars agree that raw materials are among the most important. Keohane lists raw materials ahead of other sources including capital, markets and competitive advantage in the production of highly valued goods.[5] Similarly, Krasner argues that raw materials are intimately connected with the effective functioning of the economy, the well-being of individual citizens and the

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[2] Robert Keohane, 'Realists, Neorealists and the Study of World Politics,' in Keohane, ed., *Neorealism and its Critics*, p.7.

[3] John A. Hall and G. John Ikenberry, *The State* (Milton Keynes: Open University Press, 1989), pp.10-11; and Stephen D. Krasner, *Structural Conflict: Third World Against Global Liberalism* (Berkeley: University of California Press, 1985), p.3.

Neo-realists contest that states seek always and only to maximize power. Hans Morgenthau, *Politics Among Nations* (New York: Knopf, 1948); Kenneth Waltz, *Theory of International Politics* (Reading, MA: Addison-Wesley, 1979), p.118; and Robert Keohane, 'Theory of World Politics: Structural Realism and Beyond,' in Keohane, ed., *Neorealism and its Critics*, p.194.

[4] Robert Keohane, *After Hegemony, Cooperation and Discord in the World Political Economy* (Princeton, NJ: Princeton University Press, 1984), p.32; and G. John Ikenberry and Charles A. Kupchan, 'Socialization and Hegemonic Power,' *International Organization*, Vol.44, No.3, Summer 1990, p.3.

[5] Keohane, *After Hegemony*, p.32.

national defence.[6] Of the raw resources, energy is often cited as the most important for a state to control. Thucydides even mentioned the importance of energy resources, though he was referring to wheat for fuelling soldiers' bodies.[7] More recently, Susan Strange explained energy's economic importance:

> For all developed economies, whether planned, mixed or market-oriented, energy is a vital factor of production. The basic industries in every modern economy...all need large inputs of energy, whether this comes from oil, coal, gas or nuclear power. Nor can any modern economy function without transport. Road, rail, sea and air transportation are all heavy users of energy. And when there is a breakdown in the supply of power to homes and factories, a modern society comes almost to a standstill.[8]

Henry Kissinger highlighted the political and military as well as the economic importance of oil specific to the United States:

> The [1973-74] energy crisis has placed at risk all of this nation's objectives in the world. It has mortgaged our economy and made our foreign policy vulnerable to unprecedented pressures...it has also profoundly affected our national security by triggering a policy crisis of global dimensions.[9]

A states' natural response to a threat to those resources is to increase direct control, as Susan Strange points out for oil:

> After the first OPEC price rise, other states' concern with this new *problematique* of security - how to secure supplies of energy for the country's industry and transportation systems - led, as we saw, to greater state intervention in markets and to much greater diversity of

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[6] Stephen D. Krasner, *Defending the National Interest: Raw Materials Investment and U.S. Foreign Policy* (Princeton: Princeton University Press, 1978), p.52; also see Robert Rothstein, *The Weak in the World of the Strong* (New York: Columbia University Press, 1977), p.21; and John Stoessinger, *The Might of Nations*, Eighth Edition (New York: Random House, 1986), p.15.

[7] Gilpin, 'The Richness of the Tradition of Political Realism,' pp.308-9.

[8] Susan Strange, *States and Markets* (London: Pinter Publishers, 1988), p.186.

[9] As quoted in Strange, *States and Markets*, p.201.

state policies towards energy sources other than oil.[10]

Yair Aharoni suggests that the best form of control is state ownership. He argues that state-owned companies allow governments to exert more control over resources as well as to provide invisible methods to pay largesse to different constituents. State-owned industries also permit politicians to dispense political patronage and to carry out projects which might not otherwise win legislative approval. As state owned companies also have a degree of autonomy, politicians can claim that they are free of blame if a project fails, while they are well positioned to take credit for any successes.[11] Aharoni also points out that oil ownership, in particular, enables governments to reduce dependence on multinational companies, to develop the understanding necessary to check multinational companies' activities, and to ensure inexpensive and reliable crude oil supplies.[12]

Historical evidence also supports this view. Over half of the world's state-owned oil companies existing today were created between 1970 and 1982, while states without oil (such as Japan and Germany) became more directly involved by negotiating long-term oil contracts directly with oil producing countries.[13] Britain conformed to this pattern until 1977, even creating its own state oil company in 1976. In 1977, however, Britain began to sell its oil assets, first with a tranche of British

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[10] Strange, *States and Markets*, p.202.

[11] Yair Aharoni, *The Evolution and Management of State Owned Enterprises* (Cambridge, MA: Ballinger Publishing, 1986), p.38.

[12] Aharoni, *The Evolution and Management of State Owned Enterprises*, p.103; also see Ezra N. Suleiman and John Waterbury, 'Introduction: Analysing Privatization in Industrial and Developing Countries,' in Ezra N. Suleiman and John Waterbury, eds., *The Political Economy of Public Sector Reform and Privatization* (Oxford: Westview Press, 1990), p.18.

[13] As calculated from the *Financial Times International Yearbook, Oil and Gas, 1992* (Harlow: Longman, 1992 and 1993).

Petroleum (BP) shares reducing the governments holding from 68 per cent to 51 per cent.

By 1987, the British government had sold the production portion of the British National Oil Company (BNOC), now known as Britoil, and abolished BNOC's trading operations; it had forced the British Gas Corporation (BGC) to sell all its oil assets (now known as Enterprise Oil and Wytch Farm) and had completely divested its holding in BP. In so doing, scholars and critics have argued, the British state reduced its control over a vital resource and a essential means to power. David Heald asserts: 'Through privatization measures, the government is reducing its leverage over the oil sector.'[14] Similarly, Michael Webb argues: 'The privatization of energy industries reduces the scope for the direct involvement of government in their decision taking.'[15]

1.2. Paradox of Explaining State Retrenchment

As defined by John Vickers and Vincent Wright, privatization is 'that wide range of policies designed to reduce the scope, limit the functions and generally weaken the influence of the public sector.'[16] Since the early 1980s, plans have been made for privatizations in industrialized and developing countries and by liberal as well as conservative governments, including Turkey, Nigeria, Argentina, Mexico,

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[14] David Heald, 'UK Energy Policy: Economic and Financial Control of the Nationalized Energy Industries,' *Energy Policy*, June 1981, p.107.

[15] Michael Webb, 'Energy Policy and the Privatization of the UK Energy Industries,' *Energy Policy*, February 1985, p.31.

[16] John Vickers and Vincent Wright, 'The Politics of Industrial Privatisation in Western Europe,' in John Vickers and Vincent Wright, ed., *The Politics of Privatisation in Western Europe* (London: Frank Cass, 1989), p.3.

Pakistan, India, Malaysia, Cuba, Mozambique, New Zealand, Belgium, Austria, Sweden, the Netherlands, Germany, France, Spain, Italy and Eastern Europe.[17] In fact, according to an article in the *Economist* in 1975, 'Everybody's Doing It.'[18]

Not only does the development of privatization challenge the realists' view of the state; it challenges most academics' view of the state as well. For example, Joseph Schumpeter declared in 1952 that the further expansion of public bureaucracies was 'the one certain thing about our future.'[19] Many theorists have been unable to plausibly explain the retrenchment of the state at all, as Paul Starr points out:

> Whether or not the current turn towards privatization discloses a general failure of government, it certainly discloses a general failure of social theory. From the 1950s through the 1970s, theorists of the most diverse persuasions assumed that growing welfare and regulatory states in the West and entrenched communist states in the East were accomplished facts, unlikely to be reversed or undone.[20]

Whether despite these problems, or possibly because of them, there have been

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[17] Paul Starr, 'The New Life of the Liberal State: Privatization and the Restructuring of State-Society Relations,' in Suleiman and Waterbury, eds., *The Political Economy of Public Sector Reform and Privatization*, p.35; Fariborz Ghadar, 'Oil: The Power of an Industry,' in Raymond Vernon, ed., *The Promise of Privatization: A Challenge for U.S. Policy* (New York: Council on Foreign Relations 1988), pp.231-2; William P. Glade, 'Sources and Forms of Privatization,' in Glade, ed., *State Shrinking: A Comparative Inquiry into Privatization* (Austin,TX: Institute of Latin American Studies, the University of Texas at Austin, 1986), pp.vii-ix and Chapter 1; G. John Ikenberry, 'The International Spread of Privatization Policies: Inducements, Learning and "Policy Bandwagoning",' in Suleiman and Waterbury, eds., *The Political Economy of Public Sector Reform and Privatization*, pp.88-110; and Oliver Letwin, *Privatizing the World: A Study of International Privatization in Theory and Practice* (London: Cassell Education, 1988), p.30; Suleiman and Waterbury, 'Introduction: Analysing Privatization in Industrial and Developing Countries,' pp.3-7; Colin Chapman, *Selling the Family Silver: Has Privatization Worked?* (London: Hutchinson Business Books, 1990), pp.128-30; Vickers and Wright, 'The Politics of Industrial Privatisation in Western Europe,' p.4; and search of 'privatization' in the *Financial Times* using FT profile.

[18] As quoted in Suleiman and Waterbury, 'Introduction: Analysing Privatization in Industrial and Developing Countries,' p.3.

[19] J.A. Schumpeter, *Capitalism, Socialism and Democracy* (London: Allen and Unwin, 1952), p.294.

[20] Starr, 'The New Life of the Liberal State,' p.22.

numerous attempts to explain privatization. Realists maintain that states will always prefer to control vital resources. So the only explanation for the adoption of a policy not in the states' interest is the success of 'powerful' private actors in influencing an 'uncohesive state'.[21] States with regimes that allow private actors access to the policy making process are forced to give larger shares of both sovereign largesse and entrepreneurial concessions to interest groups.[22] Merrie Gilbert Klapp analyses British oil policy from a realist perspective and argues that the British state succumbed to shipping and fishing groups as well as multinational oil companies and international banks by selling its oil assets.[23] But the evidence on privatization shows that the initiative for the sales came from political leaders themselves, and not from strong interest groups. In fact, most current accounts of privatization, from Europe to Africa, describe the obstacles leaders must overcome to implement their privatization goals rather than interest group persuading the government.[24] But realists cannot explain why a state would choose to sell and give up control of a

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[21] Eric Nordlinger, 'The Retreat of the State: Critiques,' *American Political Science Review*, Vol.82, No.3, September 1988, pp.881-3; also see Stephen D. Krasner, 'Approaches to the State: Alternative Conceptions and Historical Dynamics,' *Comparative Politics*, Vol.16, No.2, 1984; and Eric Nordlinger, *On the Autonomy of the Democratic State* (Cambridge: Harvard University Press, 1981).

[22] Raymond Vernon, *Sovereignty at Bay: The Multinational Spread of U.S. Enterprises* (New York: Basic Books, 1971); Theodore Moran, *Multinational Corporations and the Politics of Dependence: Copper in Chile* (Princeton: Princeton University Press, 1974); Brent Nelsen, *The State Offshore Petroleum, Politics and State Intervention on the British and Norwegian Continental Shelves* (London: Praeger Publishers, 1991); and Hall and Ikenberry, *The State*, pp.12-14.

[23] Merrie Gilbert Klapp, *The Sovereign Entrepreneur: Oil Policies in Advanced and Less Developed Capitalist Countries* (Ithaca: Cornell University Press, 1987).

[24] Alice Rawsthorn, 'Survey of France: So Far the Omens Are Not Ideal: Review of the Privatisation Programme,' *Financial Times*, 24 June 1993, p.III; and Tony Hawkins, 'Survey of Africa - A Continent at State: Reformers Lose Their Way - Public Sector and Privatization,' *Financial Times*, 1 September 1993, p.XI.

natural resource.

Many theories try to explain the overall retrenchment of growth with systems level solutions. Most of these type of theories identify one independent variable, such as technology, economic growth, the demands of interest groups or voters, or financial capacity. They suggest that a reversal of one or another of such external influences will cause a change in the trend of government growth.[25] While parsimonious, systems approaches do not explain why the government retrenches in some sectors and not others. More sophisticated systems approaches, such as a 'super auto reversible' model which has the benefit of incorporating several levels of variables, still cannot explain why privatization occurs in both industrial and developing countries.[26]

Elite theory explains why privatization originates from a government despite little popular demand for the policy. Elite theorists argue that the top governmental positions and therefore the national agenda are controlled by a homogenous elite, and that privatization was proposed because it meets elite goals of greater technological efficiency and was consistent with their ideological beliefs.[27] Elite theorists have trouble though explaining why the state ever nationalized industries in the first place, or why they were sold at one specific point in time.

The ideological aspect of the elites' argument has emerged as the conventional wisdom. While troublesome to scholars, the 'man on the street' in Britain easily

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[25] Christopher Hood, 'Stabilization and Cutbacks: A Catastrophe for Government Growth Theory?' *Journal of Theoretical Politics*, Vol.3, No.1, 1991, pp.43-56.

[26] Hood, 'Stabilization and Cutbacks,' pp.56-59.

[27] Ian McAlister and Donley Studlar, 'Popular Versus Elite Views of Privatization: The Case of Britain,' *Journal of Public Policy*, Vol.9, No.2, 1989, p.160, Table I; Aharoni, *The Evolution and Management of State Owned Enterprises*, p.393.

explains privatization as an ideological and party driven policy: the Labour Party with their socialist ideology nationalized Britain's industries, and the Conservatives under Margaret Thatcher, with their belief in free-markets and private enterprise, privatized Britain's industries.[28] More sophisticated accounts similarly claim that change in ideology is linked to change in state-ownership. In separate studies, Nikolaos Zahariadis and Joel Wolfe measured the correlation between the change in state-ownership and the ideology of the government in power, and postulate a strong relationship.[29] On close examination, however, this theory does not hold, even in this case of Britain where privatization is strongly associated with Thatcher's conservative ideology. In fact, both Conservative and Labour governments undertook nationalization at various points in this century, primarily to aid industries which were in real financial trouble.[30] The rationale and higher correlation, therefore, seems to have been between economic need and financial assistance rather than ideology/ As regards privatization of the oil assets, a Labour government was actually the first to privatize, with the sale of BP shares in 1977. The evidence shows a pragmatic

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[28] Aharoni, *The Evolution and Management of State Owned Enterprises*, p.317; Leo Pliatsky, *The Treasury Under Mrs. Thatcher* (Oxford: Basil Blackwell, 1989), p.107; and John Moore, 'Why Privatise?' (Speech by the Financial Secretary at the Treasury and the government minister responsible for co-ordinating the programme), November 1, 1983, in 'Privatization in the United Kingdom: Background Briefing' (London: HM Treasury, 1990), p.2; newspaper reports also add to this view, such as: Alice Rawsthorn, 'Survey of France: So Far the Omens Are Not Ideal: Review of the Privatisation Programme,' *Financial Times*, 24 June 1993, p.III.

[29] Nikolaos Zahariadis, 'Explaining Privatizations in Britain and France: A New Institutionalist Perspective,' paper presented at the American Political Science Association meeting in Washington, D.C., 30 August-1 September 1991; and Joel Wolfe, 'State Power and Ideology in Britain: Mrs Thatcher's Privatization Programme,' *Political Studies*, Vol.XXXIX, 1991.

[30] Heidrun Abromeit, 'British Privatization Policy,' *Parliamentary Affairs*, Vol.41, 1988, p.69.

evolution of a privatization programme under the Conservative government after 1979.

Pluralists argue that the form which state-owned companies take and, ultimately, their very existence is the product of struggles between state bureaucracies and interest groups (including the managers of the state-owned companies) vying for control and benefits. In this view, shifts in institutional links and relative power or political interests affect the performance or role of the state-owned companies, and relegate the role of the politician to that of merely a by-stander or referee. In the case of the oil asset sales, however, only the oil companies were passively interested in privatization. The management of BNOC and BGC were actively opposed, and the civil servants neither initiated nor opposed the sales. The primary promoters of privatization were, in fact, the politicians. Though the pluralist view that the managers of state-owned industries are a force in their own right is useful, it ignores the major source of privatization in this case - the politicians.

In conventional public choice models political leaders, bureaucrats and voter coalitions are typically characterized as having self-interested reasons for favouring expanded government,[31] yet governments do shrink as well as grow and departments expand and contract.[32] While the budget-maximizing model, for example, provides a strong explanation for the growth of government, it has traditionally been unable

[31] William A. Niskanen, *Bureaucracy and Representative Government* (Chicago: Aldine-Atherton, 1971); Patrick Dunleavy, *Democracy, Bureaucracy and Public Choice* (London: Harvester Wheatsheaf, 1991), pp.154-61; and Starr, 'The New Life of the Liberal State,' p.35.

[32] Richard Rose, *Understanding Big Government: The Programme Approach* (London: Sage Publications, 1984), p.44.

to explain state retrenchment.[33] Paul Starr sums up the problem:

> If there are self-interested reasons for political leaders, bureaucrats, and voter coalitions to favour expanded government, we need to understand how privatization ever arrived on the political agenda at all.[34]

Traditional demand side public choice explanations, such as the median voter model, fail to explain the adoption of a policy which continued to be supported only by the minority of the electorate, as privatization was. Using a supply-side public choice approach, Mariusz Mark Dobek argues in his *Political Studies* article that privatization was a politically motivated vote-maximizing policy aimed at expanding the pro-Conservative constituency. Rather than following public opinion as the traditional median-voter model predicts, Dobek's theory turns the model around and suggests that the Conservatives were attempting to lead or influence public opinion.[35] While there is some evidence that privatization provided modest electoral gains over time, there were initially no direct electoral gains, primarily because those who benefitted were already Conservative supporters.[36]

Some theorists, however, have challenged the conventional public choice orthodoxy.[37] For example, Patrick Dunleavy argues that because bureaucrats' utility

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[33] Anthony Downs, *An Economic Theory of Democracy* (New York: Harper and Row, 1957); and Niskanen, *Bureaucracy and Representative Government.*

[34] Starr, 'The New Life of the Liberal State,' p.35.

[35] Mariusz Mark Dobek, 'Privatization as a Political Priority: The British Experience,' *Political Studies*, Vol.XLI, No.1, March 1993, p.27.

[36] McAlister and Studlar, 'Popular Versus Elite Views of Privatization,' pp.170-74.

[37] Ronald Johnson and Gary Libecap, 'Agency Growth, Salaries and the Protected Bureaucrat,' *Economic Inquiry*, Vol.XXVII, July 1989; Colin Campbell and Donald Naulls, 'The Limits of the Budget-Maximizing Theory: Some Evidence from Officials' Views of Their Roles and Careers,' in André Blais and Stéphane Dion, eds., *The Budget-Maximizing Bureaucrat: Appraisals and Evidence*, (Pittsburg, PA: University of Pittsburg Press, 1991);

is not always increased with governmental growth that there are situations where bureaucrats are actually better off when governments contract.[38] By re-examining the motivations of bureaucrats, at different levels and in different types of bureaucracies, he finds that there are many situations in which bureaucrats find it in their interest not to seek increased budgets, but instead to pursue load-shedding, hiving-off and contracting-out strategies.[39] This type of flexibility suggests that the basic tenets of public choice theory are useful yet, at the same time, some of the existing assumptions need to be re-considered in light of changing circumstances. Having proved resilient to such testing so far, it is the most likely to offer scope for developing an articulated explanation for privatization.

1.3. Structure of the Thesis

This dissertation examines the British government's sale of its oil assets, some of the most important early privatizations. Instead of focusing on oil across countries, or on all privatizations within one country, I have chosen a single-sector focus, with the aim of understanding all the details and gaining the full flavour which is often lost in larger studies. My challenge, therefore, is to make sure that the conclusions here are not so specific that they pertain only to this case, but rather are transferable to other countries or other policy sectors.

Robert A. Young, 'Budget Size and Bureaucratic Careers,' in Blais and Dion, eds., *The Budget-Maximizing Bureaucrat*.

[38] Patrick Dunleavy, 'The Architecture of the British Central State, Part I: Frame Work for Analysis,' *Public Administration*, Vol. 67, Autumn 1989; Dunleavy, 'The Architecture of the British Central State, Part II: Empirical Findings,' *Public Administration*, Vol. 67, Winter 1989; and Dunleavy, *Democracy, Bureaucracy and Public Choice*, pp.174-209.

[39] Dunleavy, *Democracy, Bureaucracy and Public Choice*, pp.174-209.

Developing a Finer Grain Approach

To explain government retrenchment even in one sector, it is necessary to examine separately each factor that contributes to the ultimate decision. While the broad outcome may appear at first to be irrational (or at least difficult to explain), by examining the individual parts so that each can be understood in rational terms, the whole can also be understood. While macro level (and first principles) public choice theory proposes one explanation and uses sweeping assumptions to explain policy change, it cannot be used to explain sectoral differences. Institutional public choice models, in contrast, give a detailed account of one group of actors or one aspect of decision making and are therefore a useful tool with which to analyze each of the pieces which make up this case. Though there are many strands of public choice theory, its fundamental principles are that the individual is the central unit of analysis and that individuals are rational actors who therefore act to maximize their own utility according to the constraints they face.[40] The focus of public choice theory is the political individual: the voter, the member of an interest group, the politician and the bureaucrat. No institutional public choice theories fit this case precisely, however, so I offer variations of existing models or suggest new ones to help explain the privatization of oil in Britain. And then, though there is little precedent, I re-assemble these individual analyses into the whole.

One of the pieces often excluded from analyses of domestic policy making is the international level. Privatization, though, cannot be disconnected from the

[40] Bruno S. Frey, 'The Public Choice View of International Political Economy,' *International Organization*, Vol.38, No.1, Winter 1984, pp.201-2. For a discussion on the role of the individual see Dunleavy, *Democracy, Bureaucracy and Public Choice*, p.6.

international environment. This point is highlighted with the case of oil which, as an internationally traded commodity and the basis of a country's economic and military security, is also undisputedly a matter of high politics. But as academics in international relations know, these factors are crucial: In fact, there is a genre of international relations literature called the 'second-image reversed' which examines the impact of international level independent variables upon domestic political processes.[41] The focus of this literature, however, has been on foreign policy issues, primarily trade.[42] Public choice theories fit into the category of domestic policy making analyses and tend to ignore the international arena or at best consider

[41] Term was coined by Peter Gourevitch, 'The Second Image Reversed: the International Sources of Domestic Politics,' *International Organization*, Vol.32, No.4, Autumn 1978.

[42] Focus on general foreign policy: James Rosenau, 'Towards the Study of National-International Linkages,' in James Rosenau, ed., *Linkage Politics* (New York: Free Press, 1969); Graham T. Allison, *Essence of Decision: Explaining the Cuban Missile Crisis* (Boston: Little, Brown and Company, 1971); Jeffrey A. Frieden, 'Invested Interests: The Politics of National Economic Policies in a World of Global Finance,' *International Organization*, Vol.45, No.4, Autumn 1991; Christopher Hill, ed., *National Foreign Policies and European Political Cooperation* (London: Allen & Unwin, for the Royal Institute of International Affairs, 1983); Hill, *Cabinet Decisions on Foreign Policy: The British Experience, October 1938-June 1941* (Cambridge: Cambridge University Press, 1991); and Robert D. Putnam, 'Diplomacy and Domestic Politics: The Logic of Two-Level Games,' *International Organization*, Vol.42, No.3, Summer 1988.

Focus on trade: David Lake, *Power, Protection and Free Trade: International Sources of U.S. Commercial Strategy, 1887-1939* (Ithaca, NY: Cornell University Press, 1988); William Avery, 'U.S. Agriculture and Two-Level Bargaining in the North American Free Trade Agreement,' presented at the annual meeting of the International Studies Association, 25 March 1993; Helen V. Milner, *Resisting Protectionism: Global Industries and the Politics of International Trade* (Princeton, NJ: Princeton University Press, 1988); Ronald Rogowski, *Commerce and Coalitions: How Trade Affects Domestic Political Alignments* (Princeton: Princeton University Press, 1990); Peter Katzenstein, *Between Power and Plenty, Foreign Economic Policies of Advanced Industrial States* (Madison, WI: University of Wisconsin, 1978); and Benjamin Cohen, 'European Financial Integration and National Banking Interests,' in Paolo Guerrieri and Pier Carlo Padoan, eds., *The Political Economy of European Integration, States, Markets and Institutions* (London: Harvester Wheatsheaf, 1989).

international factors as secondary or contextual.[43] There are however a few notable exceptions which suggest that public choice theory can incorporate factors as wide ranging as international and domestic.[44]

A drawback to incorporating international level factors, as well as the domestic, is that it makes data collection and analysis unwieldy. While not exclusive to public choice theory, no effort to construct a general theoretical model has produced a parsimonious or even useful construct.[45] Simpler models, primarily two-level games, treat the state as a unitary actor and thereby ignore some of the most important domestic variables.[46] The insight of quite modest attempts to include additional factors, such as Vicki Golich's analysis of United States and European collaboration in the aircraft industry, suggest that further efforts will be

[43] Frey, 'Public Choice View of International Political Economy,' p.200; for of international variables contextually see H. Wayne Moyer and Timothy Josling, *Agricultural Policy Reform: Politics and Process in the EC and USA* (Hampstead: Harvester Wheatsheaf, 1990).

[44] John Odell and Thomas Willett, eds., *International Trade Policies: Gains from Exchange Between Economics and Political Science* (Ann Arbor: University of Michigan Press, 1990); and Cheryl Schonhardt-Bailey, 'Lessons in the Lobbying for Free Trade in Nineteenth Century Britain: To Concentrate or Not,' *American Political Science Review*, Vol.85, No.1, March 1991.

[45] Rosenau, 'Towards the Study of National-International Linkages'; and Ronen Palan, 'The Political Process in International Relations: Domestic and Global Structures,' paper presented at the British International Studies Association annual conference, Newcastle, 17-19 December 1990.

[46] Putnam, 'Diplomacy and Domestic Politics'; Avery, 'U.S. Agriculture and Two-Level Bargaining in the North American Free Trade Agreement'; Paolo Guerrieri and Pier Carlo Padoan, 'Two Level Games and Structural Adjustment: The Italian Case,' paper presented at the international conference on global and domestic factors in international cooperation, Trento 3-4 April 1989; and Jeffrey W. Knopf, 'Beyond Two-Level Games: Domestic-International Interaction in the Intermediate-Range Nuclear Forces Negotiations,' *International Organization*, Vol.47, No.4, Autumn 1993.

productive.[47] The need to extend the range of analysis beyond that of the national government or the domestic economy has been recognized,[48] and there have been many attempts to combine levels of analysis.[49] None so far, however, have accomplished the task with parsimony and accuracy.

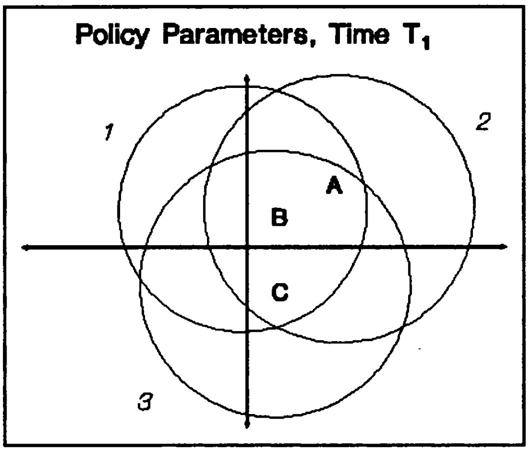

Figure 1.1.

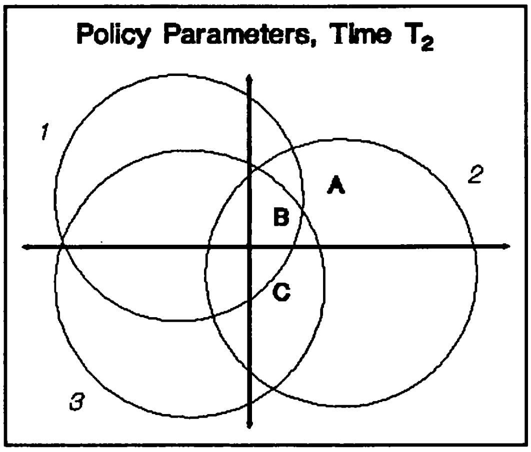

Figure 1.2.

Illustrating the approach, the various influences on policy choices can be seen as circles in a Venn diagram (see Figures 1.1 and 1.2). These influences are primarily actors' motivations and goals and the structures within which they work. On each level, these influences intersect in such a way so as to set limits to the

[47] Vicki L. Golich, 'From Competition to Collaboration: The Challenge of Commercial-Class Aircraft Manufacturing,' *International Organization*, Vol.46, No.4, Autumn 1992; also see Frieden, 'Invested Interests.'

[48] Robert Keohane, 'The World Political Economy and the Crisis of Embedded Liberalism,' in John Goldthorpe, ed., *Order and Conflict in Contemporary Capitalism* (Oxford: Clarendon Press, 1984), p.15; Gourevitch, 'The Second Image Reversed,' pp.906-7; and Allison, *Essence of Decision.*

[49] Rosenau, 'Towards the Study of National-International Linkages'; Putnam, 'Diplomacy and Domestic Politics: the Logic of Two-Level Games'; Palan, 'The Political Process in International Relations: Domestic and Global Structures'; G.John Ikenberry, David A. Lake and Michael Mastanduno, 'Introduction: Approaches to Explaining American Foreign Economic Policy,' *International Organization*, Vol.42, No.4, Autumn 1988; Helen V. Milner, 'Domestic and International Sources of Cooperation: Oil Politics in the 1940s and 1970s,' paper given at the Ford Foundation conference on the domestic and international sources of international economic cooperation, Milan, 3-4 April 1989; and Cohen, 'European Financial Integration and National Banking Interests.'

government's policy options. Because these influences can change over time, they change the options available to policy makers, increasing the possibilities as well as restricting them. The area of overlap of these parameters, therefore, illustrate which policies are possible.

In the Venn diagram, an infinite number of policies exist on a plane: three are represented here by points A, B and C. The circles 1, 2 and 3 each represent parameters within which a given set of policy options is possible, and which move and change over time. Only the area in which the parameters all overlap is a given policy option possible: the points in the overlap are the possible combinations of policies which could be implemented for that given level of analysis. As shown in Figure 1.1, at one point in time T_1, circles 1, 2, and 3 overlap so that policies A, B and C are all possible. As shown in Figure 1.2, at time T_2 in the future, however, the circles have moved so that of these three options, only policy B is now possible.

This examination of influences will be conducted on four levels, starting first with the international environment, followed by the nationalized oil companies, then the civil service (or governmental bureaucracy) and finally the British political system. To illustrate the connection between levels, imagine a

Figure 1.3.
Layers of Constraints to Policy Making

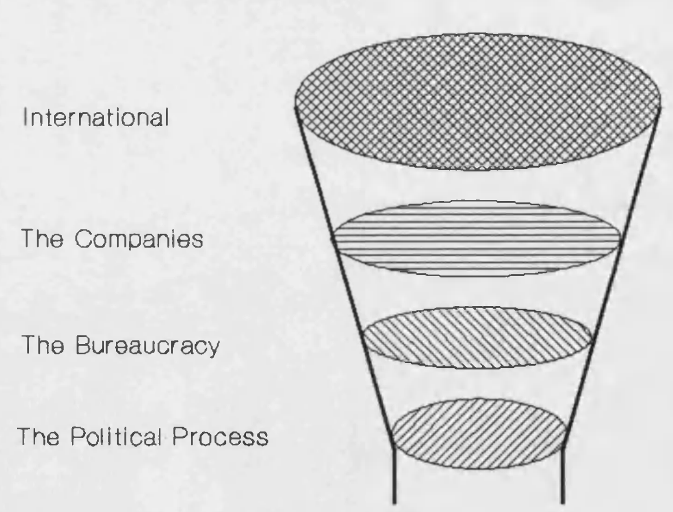

Figure 1.3.

funnel, with the broadest set of options around the ring at the top, and in which the options are narrowed as progressive sets of constraints are added (see Figure 1.3).[50]

Methodology

To explore the four levels outlined above, I relied primarily on first hand interviews, but also memoirs, newspaper accounts, public opinion polls and secondary sources for background information. Compilation of this information was facilitated by the use of a qualitative research programme. Using predictions of existing theories, focused on the relevant level, as a point of departure, I weighed the evidence and in most cases found them unsatisfactory. Using the basic premises of public choice theory and my findings, I suggest alternative explanations. Before outlining the structure of the thesis, I briefly describe the sources used in this study (for an in depth explanation see Appendix III: Research Methods).

Of the 70 people I approached, 54 agreed to meet with me, including many of the key actors involved in the sales of the government oil assets. Of those who declined, Margaret Thatcher, Geoffrey Howe and Tony Benn were the most disappointing. Thatcher, in particular, would have been an important addition but she declined despite two attempts to get her on record.

In addition to the interviews, I used a number of other sources including company annual reports, government publications, and the memoirs of some of the key figures, as well as systematic searches for relevant articles in the *Times*, the

[50] The image, but not the interpretation, comes from Charles Kegley and Eugene Wittkopf, *American Foreign Policy: Pattern and Process*, Fourth Edition (Basingstoke: Macmillan Education, 1991), p.13 - Figure 2.1: The Sources of American Foreign Policy as a Funnel of Causality.

Financial Times, the *Economist*, and the *Petroleum Economist*, as well as *Hansard Parliamentary Debates*. I used secondary sources primarily for background information on numerous aspects that I incorporate through the four levels.

To aid in the collation of this information and to cross check sources, I used the qualitative computer analysis programme, NUDIST.[51] With each source of information, I labelled each paragraph or point made in the interview with key word, and then conducted searches using these key words in order to create a pool of interview information on particular topics. In this way I was able to gather together all the information on that topic and systematically compare facts and opinions. This was more useful than note cards because there was no limit to the amount of information which could be included on a point, nor to the number of categories under which a point could be listed.

The other types of existing literature that I employed were public opinion polls. While they are used frequently by many academics, in this study I looked both at what was recorded and what was not recorded, specifically when and whether public opinion polls were held on privatization or state ownership and the intensity of that opinion. This entailed searching methodically through MORI and Gallup Polls of British Public Opinion from 1976 to 1988. I also recorded general public opinion trends on issues, leaders and parties every six months from 1976 to 1988. By looking systematically through these polls, I realized that privatization seldom merited a single question or a mention on the list of most important issues - creating a very different

[51] 'NUDIST,' which stands for Non-numerical Unstructured Data Indexing, Searching and Theorising, was developed by Thomas Richards, Lyn Richards, Joan McGalliard and Boyd Sharrock at La Trobe University, Burndoora, Australia. References: *NUDIST 2.3 User Manual*; and *NUDIST 2.3 Reference Manual*, 1992.

impression than the responses to the occasional poll revealed.

Outline of the Dissertation

After developing the theoretical perspective and outlining the general case in this first chapter, I give a brief historical overview of the British government's involvement in the oil industry in **Chapter Two.** I examine the four phases of British government involvement in the oil industry, beginning in 1914 with its initial investment in the Anglo-Persian Oil Company, as British Petroleum was then known. The first period ends with the expansion in the use of oil from military to economic following World War II. The second phase is highlighted by oil crises, Britain's withdrawal from the Middle East and the increase in domestic demand for oil. The third phase is dominated by the discovery of oil in the North Sea and the British government's initial efforts to encourage investment there in response to the rise of the threat from the Organization of Petroleum Exporting Countries (OPEC) and vulnerability abroad. The last phase is marked by Britain's concern for control of the North Sea and for capturing all possible economic rents, and is marked by the lack of major supply crises.

Turning to the specifics of this case, in **Chapter Three** I examine the details of the sale of Britain's oil assets; how they evolved from the first sale of BP shares in 1977 to three further tranches as well as the sales of Britoil, Enterprise Oil and Wytch Farm. The sales were completed between 1977 and 1987 and were 9 in number, raising £8.5 billion for the Treasury at a cost of over £224 million.

In **Chapter Four** I adapt variables from realists' systems models in order to identify areas where the British government was susceptible to international pressures.

This chapter examines three factors, two suggested by Britain's position in the international system, the international economy and the structure of the oil industry; and the other suggested by neo-liberalist literature, Britain's membership in international organizations. The focus of the investigation is on whether and how these factors affected the British government's decision to sell its oil assets.

In **Chapter Five** I analyze a group of public sector employees, the managers of state-owned companies. Though often listed in the literature on privatization as a possible obstacle to privatization, little work has been done to explain why or how these managers opposed privatization. Using the different reactions of the managers of BP, BNOC and BGC, I compare their structural features, and then explore how organizational autonomy, financial independence and success in achieving the company's mission affected the managers response to privatization proposals.

In **Chapter Six** I explore alternatives to budget-maximizing theories to explain why civil servants in the Department of Energy did not resist privatization collectively, but rather accepted or aided it at the individual level. I focus on the importance of work tasks, career-maximizing strategies, the flexibility of the British bureaucratic structure and the strength of the departments to explain their actions.

Next, in **Chapter Seven**, after establishing that public demand for privatization was weak, I examine the supply-side of the British political process. The two primary factors I identify are the role of policy entrepreneurs and strategies for party political advantage. I examine the calculation politicians made, both personally as policy entrepreneurs of privatization, and also in party political terms, including the distribution of costs and benefits to opponents and supporters over the short and long-term, and the position and intensity of party members towards privatization.

In **Chapter Eight**, I re-consider the basic question: why would a government (or anyone) sell an asset. I review the implications of the findings for the international level and the domestic level, and the calculus of the three sets of actors - the state-owned companies, the civil service and the political process. Next I consider the broader ramifications of the empirical findings for other privatizations and for better government. Finally I conclude with a discussion on the findings of this case as a whole.

Chapter Two: The Build Up of the British Government's Involvement in Oil

The sale of the British government's oil assets occurred at the end of a long history of government involvement in the oil industry. This chapter provides an overview of how the government came to own oil assets and sets the stage for the government's decision to sell them. The British government's involvement in the oil industry can be divided into four phases:

- The first phase, 1900 through World War II, includes the rise and then dominance of a few large international oil companies; it is marked by the government's investment in the Anglo-Persian Oil Company (APOC) which became the Anglo-Iranian Oil Company (AIOC) in 1935 and finally British Petroleum (BP) in 1954.

- The second phase, the 1950s and 1960s, includes the decline of Britain's influence in the Middle East at the same time demand for and reliance on oil in Britain continued to grow.

- The third phase, which overlaps with the second, runs from the mid-1960s to the mid-1970s. It is dominated on the one hand by the rise of OPEC and the government's recognition of Britain's vulnerability in terms of oil and, on the other by the discovery of oil in the North Sea and the British government's initial efforts to encourage investment there.

- The last phase, from the mid-1970s through the 1980s, includes the increase in domestic production in the wake of price rises and corresponding increases in company profits and government tax revenue, and is marked by the lack of major supply problems in Britain.

2.1. The Beginnings of Anglo-Persian and the Majors

In the early 1900s oil became an issue for the British government, not for economic reasons (coal was still the dominant fuel for transportation and industry), but because oil had been proven to be the technically superior military fuel for the Navy. A faster and more powerful fleet was vital for the Navy as it entered an arms race with Germany.[1] Reliance on oil presented risks because there were no established sources of oil either in the British Isles or the empire, unlike the abundant domestic supply of hard smokeless coal.[2] Exacerbating the problem was the fact that most of the regions where oil was found were politically unstable.[3]

Britain's First Investment in Oil

Ownership of an oil company was a desirable option for the government because Britain believed its largest suppliers, the American Standard Oil Company and Shell, had a virtual monopoly on the industry world-wide, the only other company being the British owned Burmah Oil operating in India. This opinion was reinforced by the ever increasing price of oil. The monopoly situation was doubly

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[1] Oil had three distinct advantages over coal in terms of military use. Oil had a higher thermal efficiency, it could be transferred for refuelling while at sea, and it was easier to store. Ian O. Lesser, *Resources and Strategy* (London: Macmillan Press, 1989), pp.25-6; also see Winston Churchill, *The World Crisis 1911-1914* (London: Thornton Butterworth, 1923), pp.129 and p.134; and Daniel Yergin, *The Prize: The Epic Quest for Oil, Money and Power* (New York: Simon and Schuster, 1991), pp.152-3.

[2] Lesser, *Resources and Strategy*, p.25.

[3] *Hansard Parliamentary Debates (Commons)*, 17 July 1913, col.1519, and 17 June 1914, col.1210; 'Navy and Fuel Oil,' The *Statist*, 30 May 1914, p.708; and Geoffrey Jones, *The State and the Emergence of the British Oil Industry* (London: Macmillan Press, 1981), p.12.

feared because Shell was thought to be under the control of the Germans, although this later proved to be untrue.[4] The Foreign Office was also interested in oil ownership as a means to help stabilize and control the politically sensitive and strategically important area of Persia then under threat from Russian intervention.[5]

The young, privately held Anglo-Persian Oil Company was eager to have government investment in exploration.[6] In addition to direct financial investment, the government could guarantee to purchase APOC's oil, thereby alleviating concern for sales channels for its production, which was a real problem at the time because of stiff competition from Standard Oil and Shell.[7] In addition, the government could help protect APOC's foreign operations.[8] So in 1903 APOC applied for a loan from the British Admiralty, with the support of the Foreign Office. The problem, however, was that the government was wary of the financial commitment (foreshadowing problems to come), and the Chancellor of the Exchequer turned it down.[9] A few years later, at the behest of the Foreign Office and the Admiralty, an arrangement was made with Burmah Oil Company to finance APOC, whereby in April 1908,

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[4] Jones, *The State and the Emergence of the British Oil Industry*, p.12; 'Navy and Fuel Oil,' The *Statist*, 30 May 1914, p.708; B.S. McBeth, *British Oil Policy 1919-1939* (London: Frank Cass, 1985), p.8; and *Hansard Parliamentary Debates (Commons)*, 17 June 1914, col.1160 and col.1216; and 7 July 1914, col.1033.

[5] Yergin, *The Prize*, pp.136-41; 'The Debate on Persian Oil,' *Economist*, 20 June 1914, pp.1484-5; and *Hansard Parliamentary Debates (Commons)*, 29 June 1914, col.67.

[6] His initial cost estimate was £10,000; within four years he had spent over £200,000. Yergin, *The Prize*, p.138.

[7] McBeth, *British Oil Policy 1919-1939*, p.12.

[8] *Hansard Parliamentary Debates (Commons)*, 17 June 1914, col.1197.

[9] Yergin, *The Prize*, pp.136-41; 'The Debate on Persian Oil,' *Economist*, 20 June 1914, pp.1484-5; and *Hansard Parliamentary Debates (Commons)*, 29 June 1914, col.67.

APOC became a public company, with Burmah Oil as the majority shareholder.[10] Oil was finally struck in Persia in May 1908, but due to increasing costs, APOC was again in serious financial trouble by 1913.

The government's objectives remained to have a wide geographical distribution of sources of oil, independent oil competition, and supplies from areas under British control.[11] At the time of APOC's new troubles, the government was re-considering its options, which included:

- Purchase oil fields directly, though the government had no expertise in the oil business nor any precedent for such involvement in the industry.
- Secure a loan for APOC, despite the fact that its previous efforts had proved to be insufficient to ensure the independence of the company.
- Find another oil company to support. But the only other British company was Burmah Oil, which had already invested in Anglo-Persian at the government's request.
- Continue to rely on the free market.[12]

The government finally acted when APOC's worsening financial crisis caused it to consider merging with Shell. The government agreed in May 1914 to become a partner in APOC. While over 50 per cent of APOC's shares remained in private hands, the company's Articles of Association limited the government's role to

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[10] Yergin, *The Prize*, pp.141-8; P.A. Stockil, 'A Brief History of the British Petroleum Company Limited,' *Our Industry Petroleum* (London: British Petroleum Company, 1970), p.474; and McBeth, *British Oil Policy 1919-1939*, p.6.

[11] *Hansard Parliamentary Debates (Commons)*, 17 July 1913, col.1572.

[12] R.W. Ferrier, *The History of the British Petroleum Company: The Developing Years 1901-1932* (London: Cambridge University Press, 1982), pp.180-1; and J.R.L. Anderson, *East of Suez: A Study of Britain's Greatest Trading Enterprise* (London: Hodder & Stoughton, 1969), pp.39-42.

appointing two directors to the board and a veto power. In the next few years, as APOC's financial demands rose, the government's shareholding increased to two-thirds but their role remained the same as confirmed in a letter from the Treasury signed by John Bradbury in May 1914 (see Appendix I).[13]

The government's decision was not reached without controversy. Winston Churchill, as First Lord of the Admiralty, was one of the strongest advocates. He argued that the government's investment in APOC

> has not only secured to the Navy a very substantial proportion of its oil supply, but has led to the acquisition by the government of a controlling share in oil properties and interests which are at present valued at scores of millions sterling, and also to very considerable economies, which are still continuing, in the purchase price of Admiralty oil.[14]

The opposition included economists deprecating naval expenditure, members of mining constituencies and oil executives objecting to a national inroad upon their monopolies, Conservatives disapproving of state trading, and partisan opponents denouncing the project as an unwarranted gamble with public money.[15] There were also those who objected to the reallocation of a Naval budget surplus to finance the investment, and the avoidance of proper Parliamentary debate.[16] Interestingly, many of the arguments against the government's plan were restated in the 1970s when the

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[13] Ferrier, *The History of the British Petroleum Company*, p.191 and p.199; and McBeth, *British Oil Policy 1919-1939*, p.8.

[14] Churchill, *The World Crisis 1911-1914*, p.134.

[15] Churchill, *The World Crisis 1911-1914*, p.172; also see Ferrier, *The History of the British Petroleum Company*, pp.169-70. For examples of such arguments see *Hansard Parliamentary Debates (Commons)*, 17 July 1913, 17 June 1914, 26 June 1914; 7 July 1914; *Hansard Parliamentary Debates (Lords)*, 5 August 1913; and *Economist*, 26 July 1913, pp.159-60, and 13 May 1914, p.1315.

[16] *Hansard Parliamentary Debates (Commons)*, 17 June 1914, col.1178, col.1191, col.1208, col.1224-5, and col.1243.

government established the British National Oil Company. Opposition was not intense, however, not even from the coal industry, which felt that the oil industry in general and APOC in particular were small and did not represent a substantial threat to their interests.[17]

The First Sale?

While the Navy received preferential prices for its oil, there is no evidence of government interference with the company's operations, except in its reluctance to provide additional capital.[18] This, however, was a major point of contention between APOC and the government throughout their relationship and APOC's continual pressure on the Treasury for more capital helped to bring the matter of government ownership of APOC to the fore in the early 1920s and again in the mid-1950s.

The issue was brought to a head by APOC itself when they proposed in July 1921 that they merge with Royal Dutch/Shell. APOC argued that Britain would

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[17] The reasons were threefold: total oil consumption was less than one percent of coal consumption in 1913, the industry was maintaining a 10% rate of profit, and the position of individual miners continued to improve, both in terms of pay and safety regulations. Political and Economic Policy Industry Group (PEPIG), *Report on the British Coal Industry* (London: Political and Economic Policy, February 1936), pp.115-6; B.R. Mitchell, *Economic Development of the British Coal Industry 1800-1914* (London: Cambridge University Press, 1984), p.304; Neal Buxtem, *The Economic Development of the British Coal Industry* (London: Batsford Academy, 1978), p.155 and pp.162-3; Roy Gregory, *The Miners and British Politics, 1906-1914* (Oxford: Oxford University Press, 1968), pp.97-177; and H. Stanley Jevons, *The British Coal Trade* (New York: Augustus M. Kelley, Publishers, 1969), pp.694-5.

[18] The only possible exception was Anglo-Persian's acquisition of the dying Scottish shale oil industry, though it is possible Anglo-Persian would have done so anyway because though the small independent operators were not profitable on their own, they were collectively with additional crude from Persia. The company was able to run the refineries at full capacity and therefore at a small profit until 1964. British Petroleum Company Ltd., *Our Industry Petroleum*, (London: British Petroleum Company, 1970), p.23; and *Hansard Parliamentary Debates (Commons)*, 19 November 1925, vol.188, col.576-7, and 4 December 1925, vol.188, col.2713.

benefit because for the first time a majority of Shell (50.2 per cent) would be British held, and the Treasury would save money at a time when cash demands on the Treasury were heavy.[19] The idea was rejected in a Cabinet meeting that year. Stanley Baldwin, the President of the Board of Trade, told APOC and Shell that the Cabinet had decided on purely political grounds. The government simply could not face a lobby of those opposed to monopolies; it was asking for trouble.[20]

Shell and Burmah Oil continued to push the idea, which was given a brief reprieve with the enlistment of Winston Churchill, then out of government, to lobby for them. Churchill was persuasive with the Prime Minister on the financial side: APOC's profits had declined by a third since 1920-21 and the dividend was halved, so a sale would bring the hard-pressed Treasury a welcome windfall of £20 million. When an election was announced, however, Churchill withdrew from the negotiations. With opposition from the Admiralty (because 40 per cent of naval fuel was supplied by APOC) and the Labour Party, the idea was again defeated in Cabinet at the beginning of 1924.[21] Figure 2.1 illustrates the attention the issue received in the House of Commons.

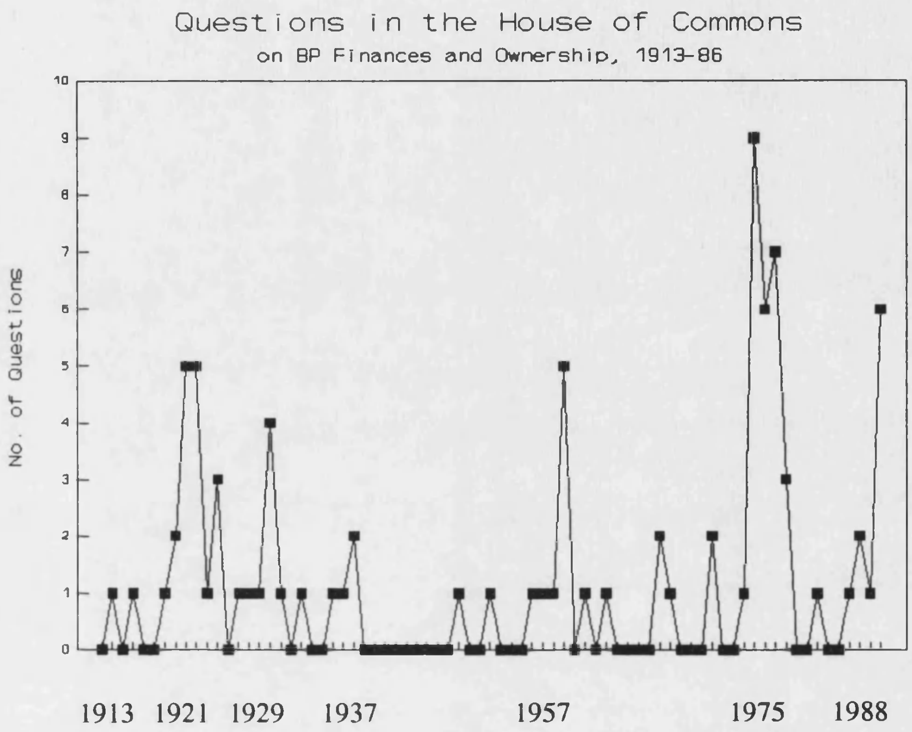
A second set of deliberations occurred in the 1950s. Though the government had just reconfirmed its existing arrangement with AIOC (which APOC became in 1935) in a letter from the Treasury on 12 April 1951, signed by Edward Bridges (see

[19] T.A.B. Corley, *A History of the Burmah Oil Company, Vol.II, 1924-1966* (London: William Heineman, 1988), pp.291-6.

[20] Corley, *A History of the Burmah Oil Company*, p.297; also see Ferrier, *The History of the British Petroleum Company*, p.250.

[21] Corley, *A History of the Burmah Oil Company*, pp.298-306; and diary entry, 29 September 1923 as recorded in John Barnes and David Nicholson, eds., *The Leo Amery Diaries: Vol.I 1986-1929* (London: Hutchinson, 1980), pp.346-7.

Figure 2.1.



Source: compiled from *Hansard Parliamentary Debates*, 1913-1988.

Appendix II), there were rumours in 1953 that they wanted to sell their 56 per cent shareholding. Though a buyer - an insurance company - was even specified, nothing happened. The rumours re-emerged in 1957 and five questions were asked in the House of Commons about the government's holding in AIOC (see Figure 2.1). But when Burmah Oil, who thought they had a verbal agreement for the right of first refusal on BP shares, asked the Chancellor, he denied that the government was considering a sale.[22] Nothing further transpired.

2.2. Decline in Britain's Control of Oil, the Rise in Domestic Demand

The second phase, which coincided with Britain's withdrawal from the Middle East and its declining position as a great power, is marked by the government's reduced ability to protect BP's interests in the Middle East. The limits to British government assistance were first realized in the Iranian crisis in 1950 and were made more evident by the Suez crisis in 1956. At the same time, demand for oil in Britain was growing.

The First Iranian Crisis

As a symbol of imperialism and a valuable national asset, AIOC became the focus of the Iranians' wrath following a coup by the nationalists led by Mohammed Mossadegh in 1950. The first directive of the new leader was to nationalize AIOC.[23] Britain and the United States, as the home governments of the oil companies based in the Middle East and the largest consumers of Middle East oil, actively worked to install a more sympathetic government in Teheran.[24] The first step against Iran was to immediately implement an oil embargo against Iranian oil exports. In order not to

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[22] Corley, *A History of the Burmah Oil Company*, p.284.

[23] K.A.D.Inglis (senior economic advisor at BP), 'The International Oil Industry - Government Involvement Through Regulation and Participation,' in Maurice Scarlett, ed., *Consequences of Offshore Oil and Gas - Norway, Scotland and Newfoundland* (St.Johns, Nfld: Institute of Social and Economic Research) 1977, pp.34-6; Anderson, *East of Suez*, pp.46-8; and Pierre Terzian, (translated by Michael Pallis), *OPEC: The Inside Story*, (Zed Books, 1973).

[24] William Hall, 'FT Report of BP: A Colourful World Player,' *Financial Times*, 19 October 1987, p.16; Yergin, *The Prize*, pp.458-70; Terzian, *OPEC: The Inside Story*, p.13; and interview with BP executive.

hurt themselves, the British and United States created a voluntary committee of oil companies and consumer countries to coordinate supply so that the vital supplies for the Korean War were not interrupted. Iranian output dropped from 660,000 barrels per day (b/d) in 1950 to 20,000 b/d in 1952. World production, however, actually increased over the same time period from 10.9 million b/d to 13.0 million b/d, so that only Iran's oil revenues were affected, in the end.[25]

Although AIOC received extensive assistance, there was a limit to what the British government could do to help AIOC regain its previous dominant position in Iran after Mossadegh was overthrown in 1953. Reflecting Britain's decreasing power and the United States and Middle East countries' increasing role, an agreement was finally reached where Iranian oil assets remained in the possession of the National Iranian Oil Company, and the management of the oil operations was contracted out to an international consortium of which AIOC received 40 per cent, the Aramco partners - Jersey, Socony, Texaco and Standard of California - plus Gulf received 8 per cent each, Shell received 14 per cent, and the French company CFP received 6 per cent.[26] Although the Iranians rejected any compensation to the British, the other members of the consortium paid AIOC $90 million for the 60 per cent rights the company was said to be giving up.[27] Thereafter, AIOC began to set up its own marketing network and soon developed into a fully integrated oil company, but it continued to produce more oil than it could market itself and sold the excess through

[25] Yergin, *The Prize*, p.464.

[26] Anderson, *East of Suez*, pp.58-9.

[27] Yergin, *The Prize*, p.478.

long-term contracts.[28]

The Suez Crisis

The decline of Britain's role in the Middle East and the rise of the United States and the Middle East countries' role was further marked by the Suez crisis of 1956. The canal was British owned and vital to Europe (in 1955, for example, two-thirds of Europe's oil passed through the Canal). On 26 July 1955, Colonel Gamal Abdel Nasser of Egypt announced its expropriation. The implications were later spelled out by the Foreign Minister Anthony Eden: 'We could not live without oil and... we had no intention of being strangled to death.' Nor could Britain's fragile balance of payments position afford the loss of foreign earnings from the Canal. In addition, a defeat would have had a demoralizing effect on Britain's already eroding international prestige.[29] Britain could not defend the Suez Canal, however, even with the help of European partners, and the United States was not prepared to take over control of the canal or to aid in its defense.[30] The British, French and Israelis felt they were left with no option but to attack Egypt on their own. Without the backing of the United States, even in the form of additional oil supplies, Europe was left on the verge of an energy crisis. A full-scale war was averted, however, when the United States negotiated British and French withdrawal in exchange for desperately

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[28] Interview with BP executive.

[29] Anthony Eden, *Full Circle* (London: Cassell, 1960), p.401; and Yergin, *The Prize*, p.485.

[30] Robert Engler, *The Politics of Oil: A Study of Private Power and Democratic Direction* (New York: Macmillan, 1961), p.261.

needed supplies of oil and financial backing.[31]

In response to the changing world political hierarchy and oil industry structure, the British government was forced to employ new strategies. The crises, and most importantly their associated costs, initiated the withdrawal of British forces from the Middle East which was to be completed by 1971. In terms of AIOC's relationship with the government, Britain's impotence, demonstrated during the Suez crisis, marked a change in what the government was able to offer AIOC, namely the protection of AIOC's Middle East operations.[32]

A False Sense of Security

The government continued to rely on the private oil industry and the AIOC through the post World War II period. Though the government responded to the increasing importance of oil by forming governmental committees and bureaus, these were uncoordinated and located in various departments.[33] Despite the changes of government and corresponding political ideologies, government relations with BP (as AIOC had become in 1954) remained virtually the same. As part of a post-war reconstruction programme, the government embarked on a series of nationalizations, but ministers did not seek to increase their control over AIOC.[34] In addition, the government protected both the domestic coal industry and the oil companies until

[31] Yergin, *The Prize*, pp.489-90.

[32] Edward Chester, *United States Oil Policy and Diplomacy* (London: Greenwood Press, 1983), pp.98-9; and Engler, *The Politics of Oil*, pp.260-4.

[33] Ferrier, *The History of the British Petroleum Company*, p.223 and p.247.

[34] *Hansard Parliamentary Debates (Commons)*, 22 December 1920, vol.136, col.1757-8.

1960.[35] Thereafter, the government continued to allow the major oil companies to command the best terminal and storage facilities and to maintain their exclusive contracts with most filling stations.[36] Remarkably, the growth of the oil industry and the fall of oil prices during the 1950s and 1960s, overshadowed the crises and lulled oil consumers into a dependence on oil.

With prices falling and new oil discoveries being made, there was a new sense of consumer confidence, minimizing the need for governments to take security measures. The British government's confidence was illustrated by its lack of concern in 1969 when its holding in BP dropped below 50 per cent to 48.2 per cent for the first time since mid-1910s. In a business transaction, BP had issued new shares to the Distillers Company in exchange for Distillers' chemicals and plastics interests.[37] Though the Chancellor of the Exchequer James Callaghan was informed, as he put it, 'nobody made a row.'[38] It went virtually unnoticed in the House of Commons, as evidenced by the lack of questions (see Figure 2.1), nor was the percentage decline raised in the Cabinet or in public.[39]

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[35] J.E. Hartshorn, *Oil Companies and Governments, An Account of the International Oil Industry in its Political Environment* (London: Faber and Faber, 1962), pp.236-7; A.M. Newman, *Economic Organization of the British Coal Industry* (London: George Routledge, 1934), pp.439-40; and PEPIG, *Report on the British Coal Industry*, p.116.

[36] Hartshorn, *Oil Companies and Governments*, p.236.

[37] BP, *Annual Reports and Accounts*, 1969; Robert Fraser and Michael Wilson, *Privatization: The UK Experience and International Trends* (Harlow, Essex: Longman, 1988), p.51; and Anderson, *East of Suez*, p.20.

[38] As quoted in Tony Benn, *Against the Tide: Diaries 1973-76* (London: Hutchinson, 1989), p.647.

[39] *Hansard Parliamentary Debates (Commons)*, 24 October 1967, vol.751, col.428. Although the Treasury stated that they would not take any steps to restore the national holding in BP to over 50%, there were no further questions about the government's holding until 1971 and then not again until 1974.

2.3. Britain's Vulnerability and Subsequent Search for Oil Independence

Though realizing its vulnerability in terms of oil after the Suez crisis, the 1973-74 oil embargo was an even larger shock. In response, the British government sought new means to address security of supply. In so doing, the government was greatly aided by the discovery of oil in the North Sea and the increase in the price of oil which made production there financially feasible.

The 1973-74 Oil Crisis

When AOPEC, the Arab members of OPEC, enforced an oil embargo against the United States and the Netherlands, the effect on Britain was a dramatic increase in oil prices in the 1970s (see Figure 2.2) causing severe economic damage and political disruption, exacerbated by a coal miners strike in 1974. The 1973 oil crisis was a test of its long established mechanisms to ensure security of supply though reliance on BP and the private oil companies.

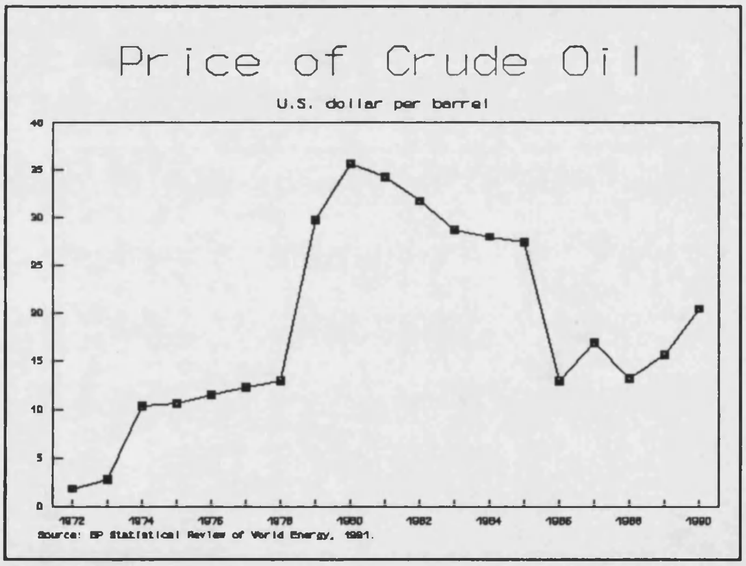

Figure 2.2.

In December 1973, Prime Minister Edward Heath asked Shell and BP to supply more oil to Britain. Eric Drake, then chairman of BP, refused the Prime Minister even though the government was its largest shareholder. Drake argued that to favour Britain could cause retaliation from other governments, and possibly even nationalization of BP operations in those countries. Therefore, as a director of the company entrusted with the welfare of all stockholders, Drake could not comply with the government's request. If the government were to pass the appropriate laws, Drake said, BP would, of course, comply. Heath, however, did not take that route and BP's directors were left to make decisions in the company's best interest.[40] Shell also refused, although 40 per cent British owned, citing the interests of its Dutch shareholders who comprised the other 60 per cent of the company.[41] At the time, as one Conservative remarked, 'Heath and half the government were amazed with BP's response.'[42] A Department of Energy minister remarked:

> Heath was horrified in 1974 to have no control over the company during the oil crisis. I inherited that cannon. The resulting feeling was that the country had to have control over its own oil.[43]

The crisis also forced Britain to decide whether to show solidarity with the EC which it had just joined, or to keep its status as a friendly country in the eyes of the Arabs. The decision was neatly taken care of by the oil companies. The British and the French decided not to put the Organization for Economic Cooperation and Development (OECD) Oil Committee oil-sharing system into action. The oil companies were the ones who provided the mechanism for oil sharing and ostensibly

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[40] Interview with BP executive; also see Guy Arnold, *Britain's Oil* (London: Hamish Hamilton, 1978), p.36; and Hans Maull, 'Oil and Influence: The Oil Weapon Examined,' in Klaus Knorr and Frank Trager, eds., *Economic Issues and National Security* (Lawrence, KA: Regents Press, 1977), p.272.

[41] Yergin, *The Prize*, pp.261-4; Arnold, *Britain's Oil*, p.36; and interview with Treasury civil servant.

[42] Interview with Department of Energy minister.

[43] Interview with Department of Energy minister.

by refusing to favour one country over another but also benefitting from the high oil prices.[44]

In the wake of these higher oil prices, the discovery of oil in the North Sea took on a new importance, as it was now desirable and economically feasible to overcome the harsh environmental conditions of the North Sea to further explore and develop oil in Britain's politically stable region.[45] The desirability is evident by the fact that more than 150 companies had invested in the North Sea by 1980, 82 of which were British.[46] In terms of security, Britain benefitted from the North Sea oil in two ways - it developed its own domestic oil supplies, and no longer relied on imports from the Middle East.

Britain's Initial North Sea Strategy

The first commercial gas discovery in the North Sea was made in 1965, and oil was discovered in November 1969.[47] Further discoveries, advances in offshore technology and vast amounts of investment made it possible for the first oil to reach the British shore on 18 June, 1975. The price rises caused by OPEC beginning in 1973 made the development of North Sea oil fields commercially viable. These advances fundamentally changed Britain's energy situation. In the space of ten years,

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[44] Maull, 'Oil and Influence,' p.271.

[45] BP, *Statistical Review of World Energy*, June 1990 and July 1989, p.4.

[46] Department of Energy, *Development of the Oil and Gas Resources of the United Kingdom* (London: HMSO, 1984); and 'UK North Sea Seventh Round,' *Petroleum Economist*, April 1981, p.164.

[47] BP made the first gas discovery. The first oil discovery was made on the Norwegian side; in December 1970 BP discovered oil in Britain in what has become the largest field, known as the Forties field.

Britain shifted from being a major oil importer to being a net oil exporter (see Figure 2.3), and from being dependent on the Middle East to being self sufficient in oil from in its own backyard.[48]

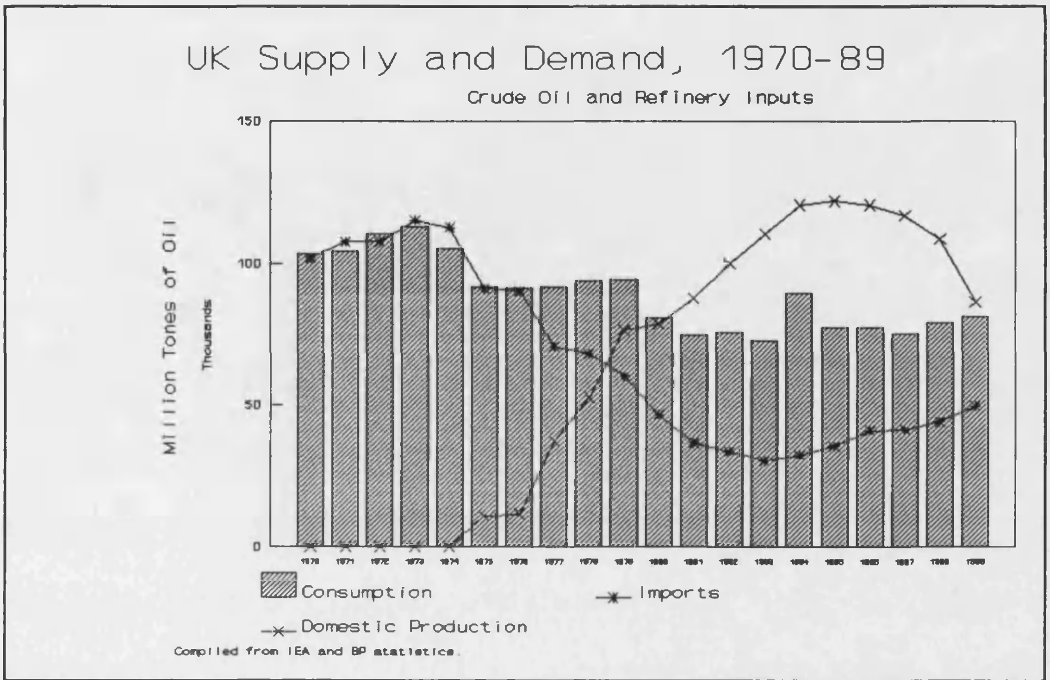

Figure 2.3.

By 1983 Britain was the sixth largest oil producer in the world, ahead of countries like Kuwait and Libya. The gross value of oil and gas from the United Kingdom Continental Shelf (UKCS), the British portion of the North Sea rose from £6.3 billion in 1979 to £18.8 billion in 1983, and as a proportion of GNP from 2.5 per cent to 5.3 per cent. Tax revenues from companies operating in the North Sea rose from £562 million in 1978-79 to £8.9 billion in 1983-84.[49] In perspective, the contribution to GDP was always less than that of the construction industry or

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[48] Because industrial economies use several kinds of crude oil, imports were still necessary, but the high quality of the North Sea oil made it profitable to export. BP, *Statistical Review of the World Oil Industry* 1980, 1989 and 1990.

[49] Includes Petroleum Revenue Tax (PRT), royalties and corporation tax. 'The North Sea's Second Wind,' *Economist*, 12 May 1984.

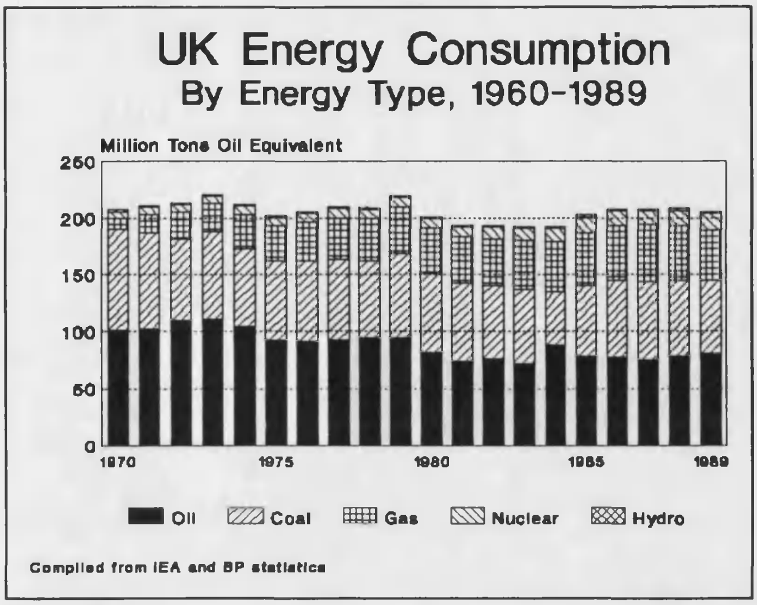

Figure 2.4.

agriculture, and the North Sea's direct effect on jobs was small because oil and gas were highly capital intensive industries. However, much of the capital invested in the North Sea came from abroad and thus was an addition to Britain's economy.[50] The overall UK energy supply situation also improved with North Sea oil production and the change in energy demand after the 1973 oil crisis. There was an overall energy surplus by 1980, with the decrease in the demand for oil and coal accounting for the majority of the decline, while demand for gas actually increased slightly and nuclear stayed the same (see Figure 2.4).[51]

The Establishment of the Department of Energy

In 1973 the House of Commons Public Accounts Committee (PAC) issued a report which criticized the government for giving away too many benefits associated with North Sea oil. With pressure mounting during the coal miners strike and the

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[50] 'Mixed Blessings from the North Sea,' *Economist*, 23 January 1982.

[51] International Energy Agency, *Energy Balances of OECD Countries 1970-1985* (Paris: IEA/OECD, 1987); Martin Quinlan, 'Mounting Energy Surplus,' *Petroleum Economist*, May 1984, pp.186-7; and Martin Quinlan, 'Coming Upheavals in Energy Supply,' *Petroleum Economist*, November 1989, p.335.

1973 oil crisis, the Conservative government created the Department of Energy (DEn) in January 1974, consolidating divisions and bureaus spread across at least three departments previously managing energy matters.[52] The new department was given a high profile with the appointment of Lord Carrington, the Tory party chairman, as Secretary of State.[53]

The DEn was an agency which spent a low proportion of its total budget on salaries, because its primary task was to channel funds to other public sector organizations, namely the nationalized energy industries.[54] The DEn also raised large amounts of finance. In 1983, for example, the receipts from royalties in the North Sea were almost £2 billion, dwarfing the department's total budget, which for the same year was £50 million.[55] As a new department with a small staff, the DEn had difficulty establishing its position versus the Treasury and the Central Policy Review Staff (CPRS) who had already established their credibility in energy matters. The DEn's public reputation was also tarnished by mistakes such as the £44 million overpayment in grants to oil companies in 1979 and the poor administrative handling

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[52] Inglis, 'The International Oil Industry.' p.49.

[53] 'The Chance to Work up a Little Heat about Energy,' *Economist*, 12 January 1974, p.83; Patrick Cosgrave, *Carrington, A Life and a Policy* (London: JM Dent, 1985); Peter Hennessy, *Whitehall* (London: Secker and Warburg, 1989), p.432 and pp.445-8; and interview with Department of Energy civil servant.

[54] Dunleavy, 'The Architecture of the British Central State, Part I,' pp.254-5; Dunleavy, 'The Architecture of the British Central State, Part II,' p.400; also see David McInnes, 'Policy Networks within the Department of Energy and Energy Policy,' Essex Papers in Politics and Government, No.82, July 1991, p.21.

[55] Supply Estimates 1983-84: Class IV: Industry, Energy, Trade and Employment, *British Parliamentary Papers*, vol.26.

of the coal miners strike in 1980.[56] By the mid-1980s, the department was in better command of the energy control apparatus, including taxation, subsidies and grants, licenses, the nationalized industries, safety and shadow prices.[57] The issue of the poor quality of the DEn staff, however, was raised again in November 1990 after the Piper Alpha disaster when the Cullen Report severely criticized the department for major safety failings. As a result, the DEn was stripped of its responsibility for offshore safety to the benefit of the Health and Safety Executive.[58] In 1993, the DEn was amalgamated into the DTI.

The other notable feature about the department was its lack of consumer or environmental orientation. There were no divisions within the department with such responsibilities. Consumers and environmentalists, therefore, had no representation within the department, and such matters were only dealt with peripherally as they affected other aspects, such as oil production.[59]

The nationalized industries were the most important feature of the department. On the one hand they were the means to control the energy sectors, but on the other they were semi-independent organizations in competition with each other. They were

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[56] Margaret Thatcher, *The Downing Street Years* (London: Harper Collins, 1993), pp.140-1; Adrian Ham, *Treasury Rules, Recurrent Themes in British Economic Policy* (London: Quartet Books, 1981), pp.40-1; Tessa Blackstone and William Plowden, *Inside the Think Tank: Advising the Cabinet 1971-1983* (London: Mandarin, 1990), pp.80-3; and interview with Department of Energy civil servant.

[57] Heald, 'UK Energy Policy,' pp.106-9; and interviews with Department of Energy civil servants.

[58] 'DEn and Oxy Pilloried by Piper Alpha Report,' *Financial Times: North Sea Letter*, 14 November 1990, p.778/1.

[59] McInnes, 'Policy Networks,' Figures 1-6; and interview with Conservative minister.

so powerful that the DEn was unable to make them cooperate or coordinate strategies.[60] For example, there was a committee of the planning directors for each industry, but as one executive who attended the only meeting between 1980 and 1982 explained, 'we couldn't agree on anything...no one wanted to reveal numbers or plans.'[61] Only the coal and nuclear industries were largely dependent on the department for funds. Electricity and gas had been raising an increasing proportion of their revenue from customers and thus were able to repay government debt and make net contributions to government funds.[62] The largest net earner under the control of the department, however, was the oil and gas industry. Therefore, despite the fact that one civil servant claimed the 'touchstone' of the department's policy was security of supply,[63] the department had few means of direct control over supply. Efforts to even articulate the DEn's policy were hampered by the persistent change in factors such as the price of oil. In the end, one civil servant lamented, it was impossible to say anything except in generalities.[64] As one nationalized industry executive said, 'the department might have argued that there was a policy, but had no means to implement it.'[65]

The evolution of policy was mirrored in the changing structure of the department's Oil Division over time. The division began by focusing on offshore

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[60] Heald, 'UK Energy Policy,' p.103.

[61] Interview with BNOC executive.

[62] Andrew Likierman, *Public Expenditure: The Public Spending Process* (London: Penguin Books, 1988), p.34; and interview with Department of Energy civil servant.

[63] Interviews with Department of Energy civil servants.

[64] Interview with CPRS official.

[65] Interview with BNOC executive.

supplies, exploration and participation agreements. Broader policy decisions and community and international policy were added in the early 1980s, until finally in 1990 responsibility for oil had become a streamlined operation of overseeing current operations and holding small licensing rounds.[66]

The Department of Energy's Influence in the Oil Industry

The DEn's primary means of controlling oil exploration and development in the North Sea were discretionary licenses and taxation. The DEn was also responsible for the offshore-supply industry, depletion policy and recording statistics. The discretionary system allowed the government to discriminate between applicants on the basis of their contributions to the North Sea development and Britain's economy, as well as to favour British companies.[67] The Treasury preferred an auction system to raise more money upfront, and an auction was tried in the fourth round in 1971 where 15 blocks were sold for £37 million and again in the eighth round in 1983 where seven blocks were sold for £33 million. With these exceptions, the discretionary system prevailed because the government decided that the power to award licenses was more valuable than the extra cash an auction might raise.[68] For example, the government used licences as a carrot in the participation negotiations.

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[66] McInnes, 'Policy Networks within the Department of Energy and Energy Policy,' Figure 1; and interview with Department of Energy civil servant.

[67] Louis Turner, 'State and Commercial Interests in North Sea Oil and Gas: Conflict and Correspondence,' in Martin Sacter and Ian Smart, eds., *The Political Implications of North Sea Oil and Gas* (Oslo: Universitetsforlaget, 1975), p.98; and Colin Robinson, 'The Errors of North Sea Policy,' *Lloyds Bank Review*, No.141, July 1981, pp.20-1.

[68] Turner, 'State and Commercial Interests in North Sea Oil and Gas,' p.95; 'Eighth Round to Include Auction,' *Petroleum Economist*, June 82, p.253; 'License Auction Raises £37 Million,' *Petroleum Economist*, March 1983, p.100; and interviews with Department of Energy civil servants.

When the threat of withholding licenses from uncooperative companies was carried out in the fifth licensing round, in the words of one DEn civil servant, 'the government's negotiating position was boosted enormously.'[69]

Of all the government's means, the tax regime affected the oil companies the most; it was a major factor in their exploration and development calculations. In 1964 the private oil companies were granted long concessions, low tax rates and few regulations to entice them to explore and develop the North Sea.[70] Once oil was discovered, risk was reduced and the future gains became apparent, and the government began to raise taxes and increase the level of regulation. Over the years, ministers and the companies negotiated back and forth. The DEn was in a disadvantageous position in the early 1980s as the price of oil began to fall, oil companies profits fell and North Sea production approached a natural decline. To induce private oil companies to develop smaller, marginal fields, the type of fields thought to be remaining, the government made new tax concessions.[71] Once the price of oil began to increase after the 1986 low, investment picked up slowly, and

[69] Interview with Department of Energy civil servant.

[70] Under the first licensing round the government charged 12.5 per cent in royalties and taxes at the corporate rate of 53.75 per cent; in 1975 the Oil Taxation Act was passed which limited tax loopholes and created a new Petroleum Revenue Tax of 45 per cent, raised to 75 per cent by 1982. And in 1981, the Supplementary Petroleum Duty was introduced and was set at 20 per cent (later replaced by the Advance Petroleum Revenue Tax.) Nelsen, *The State Offshore Petroleum, Politics*, p.20, p.55, and p.91; Alexander Kemp and David Rose, 'Tax Changes - A Lost Opportunity,' *Petroleum Economist*, April 1982, p.133; and Turner, 'State and Commercial Interests in North Sea Oil and Gas,' p.93.

[71] 'Tax Aid for Marginal Fields,' *Petroleum Economist*, July 1982, p.296; 'Distortions That Impede Recovery,' *Petroleum Economist*, September 1982, p.350; 'Budget Boost for North Sea,' *Petroleum Economist*, April 1983, pp.143-4; Alexander Kemp and David Rose, 'Tax Changes Give New Incentives,' *Petroleum Economist*, May 1983, p.163; 'Implications of Cheaper Oil,' *Petroleum Economist*, March 1983, pp.78-9; and Alexander Kemp and David Rose, 'Dangers of Reliance on Oil Revenues,' *Petroleum Economist*, March 1983, p.81.

the swing reversed.[72]

The Department of Energy also built up an expertise in taxation, which was utilized by the unusual practice of advising the Treasury. Civil servants explained that the DEn was included in the oil taxation system because the Treasury needed their knowledge.[73] The DEn was also responsible for calculating and collecting royalties, except for those paid in kind from 1977 to 1985 which BNOC then disposed of under the direction of the DEn. The involvement of the Treasury and the DEn led to disagreements over the tax rates. The Treasury wanted higher tax revenues, while the DEn was concerned that higher taxes might discourage investment and cause consumer criticism.[74]

The DEn's responsibilities for depletion policy, the offshore-supply industry and the maintenance of energy statistics were considered secondary functions compared to issuing licenses and taxation. Depletion policy was a highly contentious issue. The Treasury and the oil companies wanted oil produced as fast as possible to maintain revenues, while some in the DEn were concerned with security of supply and wanted to spread the production of oil further into the future.[75] Though options were discussed, no restrictions were placed on production. The Department of Energy took over the Offshore-Supplies Office (OSO), created by the DTI in 1973 to ensure Britain's share of the off-shore oil supply industry (all the equipment and services needed for oil exploration and development). The DEn devoted much time and effort

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[72] Martin Quinlan, '1985 - Last of the Golden Years,' *Petroleum Economist*, April 1986, p.121.

[73] Interviews with Department of Energy and Treasury civil servants.

[74] Interviews with Department of Energy and Treasury civil servants.

[75] Interviews with Department of Energy civil servants.

to the challenge and was proud of the results: 73 per cent of offshore-supply contracts (in terms of value) went to British companies compared with almost none in the mid-1970s.[76] In addition, the DEn maintained sophisticated energy statistics, but found that few outside the department ever used them.[77]

The Role of the Private Oil Companies

Despite the plethora of companies involved in the North Sea, production was

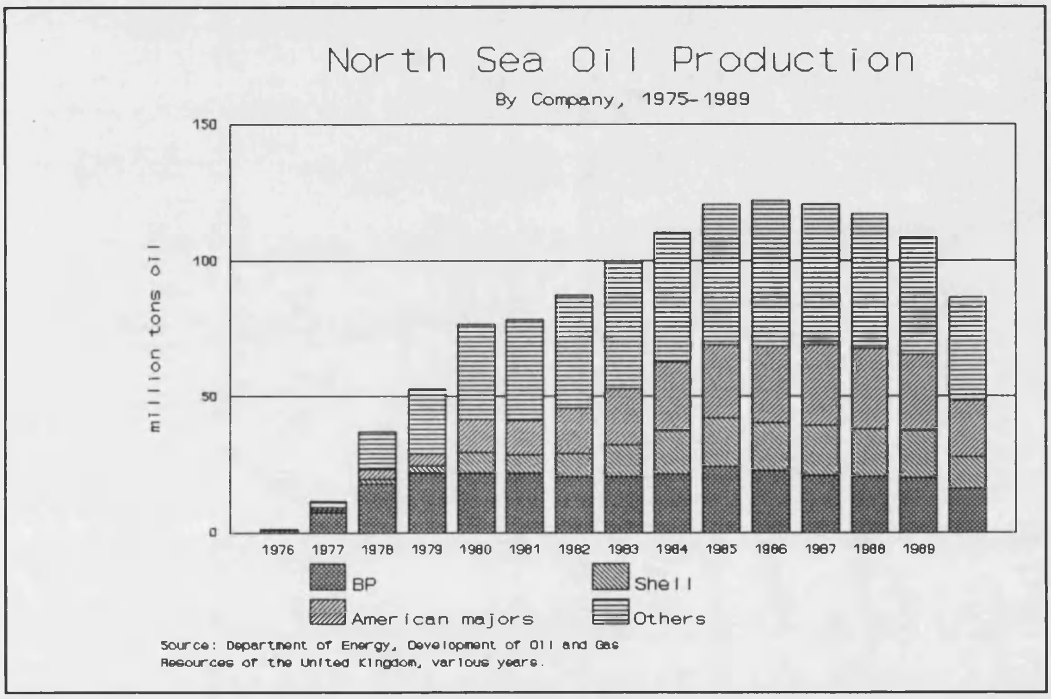

Figure 2.5.

concentrated in the hands of the majors. As shown in Figure 2.5, the seven major oil

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[76] This figure may be misleadingly high because it includes British subsidiaries of American and French companies. 'Bringing in the Catch,' *Economist*, 12 May 1984; and Michael Jenkin, *British Industry and the North Sea* (London: Macmillan, 1981), pp.63-4, p.73 and p.82.

[77] Interview with Department of Energy civil servant.

companies controlled at least 50 per cent of North Sea oil throughout its development.[78] The DEn sought to include as many companies as were capable in the development of the North Sea. As one civil servant explained, the rationale was 'the larger the array [of oil companies], the more ideas and thinking, the larger the pay-off.'[79] The small companies, however, could not meet the capital costs of developing new finds, and thus, the majors were favoured.[80] Initially, BP and Shell controlled 20 per cent and 15 per cent of the North Sea respectively, and the five American companies controlled much of the remainder. Over time, however, smaller companies increased their portion from 10 per cent in 1975 to 25 per cent by the early 1980s.[81]

The government had, in fact, always been dependent on the private oil industry. According to one civil servant:

> Despite upheavals going back to Suez, the oil industry always managed to deliver the oil - much more so than anyone gave them credit for in advance.[82]

Another pointed out that 'the department tended to look after the interests of the oil companies; it was the tradition.'[83] Through informal and formal channels at all

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[78] Department of Energy, *Development of Oil and Gas Resources*, 1984 and 1991.

[79] Interview with Department of Energy civil servants.

[80] Because Shell had a 50-50 exploration and production agreement with Esso (now Exxon) in the North Sea, the U.S. company Esso was also a beneficiary of the government's policy.'Making Waves: Attraction of Oil Investment in the North Sea,' *Economist*, 18 March 1989.

[81] The other portion went to the large independents, including Amerada Hess and Occidental Petroleum. Department of Energy, *Development of Oil and Gas Resources*, 1984 and 1991; and Arnold, *Britain's Oil*, p.42.

[82] Interview with Department of Energy civil servant.

[83] Interview with Department of Energy civil servant.

levels, DEn civil servants frequently spoke with the oil companies. As a result, most civil servants were sympathetic to or at least understood the private oil companies' positions. The DEn civil servants were proud of these good relationships. The ultimate manifestation of the DEn's concern for oil companies was their strategy guarding against excessive governmental interference; it was thought that too much interference would force the companies to go elsewhere.[84] According to one civil servant:

> The government was continually turning the screw tighter to see what happened until finally in 1981 they went too far and there was a down turn [in development], and the policies were then reversed.'[85]

As another civil servant explained, 'the department was too soft sometimes [on the oil companies]...but in the end, we still had to work with them.[86]

There was also a healthy dose of scepticism about the oil companies evident among civil servants in the DEn. One civil servant explained that the oil companies 'could say they were mindful of the national interest, but they were also commercial and couldn't change that.' The civil servant argued that the participation agreements were therefore necessary to override those commercial obligations.[87] Another simply explained, 'oil companies have different interests than the government and the population.'[88]

The government devised two specific means of control, participation

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[84] Interviews with Department of Energy civil servants.

[85] Interview with Department of Energy civil servant.

[86] Interview with Department of Energy civil servant.

[87] Interview with Department of Energy civil servant.

[88] Interview with Department of Energy civil servant.

agreements and assurances, as well as BNOC. Participation, as originally planned by the Labour government, was a full partnership arrangement whereby a national oil company would participate in the exploration and development, contribute 51 per cent of the expenditure and then receive 51 per cent of the production and profits. The Treasury argued that it could not fund the 51 per cent investment,[89] and the private oil companies argued that they had already invested a substantial amount of capital into the North Sea on the understanding that there would be no government interference.[90] Taking into account these obstacles, another concept of participation was developed with a national oil company. The national company would have the right to take at market price up to 51 per cent of a company's oil production, but the government assured the companies that they would be no better off and no worse off by the arrangement.[91] In practice this meant that the national oil company could buy up to 51 per cent of a company's production at market price, thereby nominally controlling 51 per cent of UK oil, and then immediately re-sell it, sometimes back to the same company. One DEn civil servant described the arrangement: 'On the surface it looked good, but it was really a bit of a wangle ... and didn't do much.'[92]

Even though the concept proved to be relatively innocuous, long negotiations ensued during the 1970s in which the government used leverage over the companies

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[89] 'New Moves to Still Fears on Oil Programme,' *Times*, 12 August 1974, p.1; and *Hansard Parliamentary Debates (Lords)*, 23 July 1975, vol.363, col.330.

[90] Harold Wilson, *The Final Term: The Labour Government 1974-76* (London: Weidenfeld and Nielson, and Michael Joseph, 1979), p.40.

[91] A.W.Baker and G.H.Daniel, 'BNOC and Privatization - The Past and the Future,' *Journal of Energy and Natural Resource Law*, Vol.1, No.3, 1983, p.149.

[92] Interview with CPRS official.

needing loan guarantees or other assistance. It took a year of negotiations before an agreement was reached with BP on 25 January 1976 at a meeting between the Prime Minister, the Secretary of State for Energy and the chairman of BP.[93] Agreement with the other major international oil companies proved more difficult; the Chairmen of Exxon and Shell were vocally antagonistic, and agreements were only achieved after the government showed its willingness to withhold licenses from a company refusing to cooperate.[94]

Another means of control, company 'assurances', was enacted in conjunction with the participation agreements. These assurances followed a similar arrangement to the one outlined in a letter from BP to the DEn obtained by the *Financial Times*. The letter stated that BP would cover any short-term gap which stopped short of a major international crisis (defined as a 7 per cent cut in supply) as long as there was 'no legal or governmental constraint on its ability to raise prices as a necessary means of recovering costs.'[95] For a price all companies would guarantee supply, at least in a short-term crisis. According to DEn civil servants, these assurances were the government's main means of securing energy supplies after BNOC was split and Britoil was sold in 1982.[96]

2.4. Direct Ownership in the North Sea

With the 1973 oil crisis, the government began to consider the idea of a

[93] Harold Wilson, *Final Term*, p.42.

[94] Interview with Department of Energy civil servant; and a review of articles in *Times*, 1974-78.

[95] 'Bringing in the Catch,' *Economist, 12 May 1984.*

[96] Interview with Department of Energy civil servants.

national oil company. The participation arrangements made a national oil company of some sort necessary. The thinking began under the Conservative government, but it was the Labour government elected in 1974 which debated more extreme options, including making BP into a fully national oil company and allowing only British companies into the North Sea.[97]

The British National Oil Company

After the 1973-74 oil crisis, Britain realized its vulnerability in terms of oil, and responded by seeking new ways to control its oil supply. The government briefly considered transforming BP into a fully government-owned company. This was made more plausible by happenstance. In January 1975, the government increased its stake in BP from 48 per cent to 68 per cent as part of a deal to aid the financially troubled Burmah Oil. An original shareholder in BP, Burmah Oil maintained a 20 per cent stake. Under the government's scheme to help the financially troubled company, Burmah sold its holding to the Bank of England (while the Treasury held the original shares) for £179 million. By March 1976, the shares were valued at £447 million, and the Burmah shareholders sued the Bank of England for improper proceedings, but eventually nothing was proved.[98] The increased holding also spurred questions in the House of Commons (see Figure 2.1), but the government responded that a decision had not yet been made, and implied that the government was at least considering the

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[97] Adrian Hamilton, *North Sea Impact, Off-Shore Oil and the British Economy* (London: International Institute for Economic Research, 1978) p.16; and interviews with BNOC and BP executives.

[98] 'Crude Solution,' *Economist*, 11 December 1976, p.119; BP, *Annual Report and Accounts*, March 1976; Benn, *Conflict of Interest*, p.75; and interviews with Treasury civil servants and BP executives.

sale of the shares.[99]

Instead of nationalizing BP, a new entity was created, the British National Oil Company (BNOC), in 1976 by Labour Party ministers who had been debating the merits of a National Hydrocarbons Corporation inside the party since 1967.[100] The arguments for and against BNOC were similar to those made about the government's initial investment in APOC. Advocates argued that BNOC would defend against the tyranny of the existing large corporations, while others focused on the general benefits to Britain's economy.[101] The existence of national oil companies in other democracies including France, Canada and Italy diffused the accusations of extreme socialism.[102] The opposition included the coal industry which feared that government support would divert their customers to oil, Conservatives against government involvement in industry and the oil companies who believed that BNOC would impede their development of the North Sea at a crucial time.[103] Yet, as one BP director said:

> We are in partnership with governments of all political complexions all over the world. We are unlikely to be frightened off by anything the Labour government has in mind. In any case our investment [in the

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[99] *Hansard Parliamentary Debates (Commons)*, 6-21 February 1975, 16 May 1975, 30 June 1975, 17 October 1975, 12-26 January 1976, 20 February, and 24-5 March 1975.

[100] D. Hann, 'The Process of Government and UK Oil Participation Policy,' *Energy Policy*, June 1986, p.254.

[101] *Hansard Parliamentary Debates (Lords)*, 23 July 1975, vol.363, col.327-347; and interview with BNOC executive.

[102] Interview with Department of Energy civil servant.

[103] Inglis, 'The International Oil Industry,' p.52; Philip Shelbourne, 'BNOC's Growth and Prospects,' *Coal and Energy Quarterly*, No.30, April 1981, p.3; also see articles from the *Times* on the creation of BNOC, including: 5 June 1975, p.22; 25 June 1975 Special Report, p.IV; 13 July 1975, p.17; 10 August 1975, p.15; 13 November 1975, p.19; and 30 November 1975, p.7.

North Sea] is now too big. It would be too late to stop [producing] even if we wanted to.[104]

Opponents' fears were highlighted because BNOC was created partly under the direction of two Labour leaders who strongly believed in state-ownership - Tony Benn, Secretary of State for Energy from 1976-79, and Tommy Balogh, a former Member of the Economic and Financial Committee of the Labour Party and Minister of State in the DEn from 1974-75 who became deputy chairman of BNOC from 1976-78.[105]

BNOC was created to serve two sometimes contradictory roles. First it was an information-gathering, monitoring and advisory agent.[106] Second it was a commercial oil production and trading company. BNOC thus had the dual role of competing against private oil companies in the North Sea as well as advising their regulators, and many saw these functions as contradictory. One BNOC executive found that fear of a 'spy in the camp' was second only to fear of technical incompetence as reasons why private companies did not want to work with BNOC.[107] The management argued that BNOC was not a regulatory agency, only an advisor to the government, and a 'Chinese Wall' had been erected between the operations side and the rest.[108]

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[104] As quoted in Harold Wilson, *Final Term*, p.40.

[105] Interviews with Department of Energy civil servants and BNOC executives.

[106] John Vickers and George Yarrow, *Privatization: An Economic Analysis* (Cambridge, MA: MIT Press, 1988), p.323.

[107] Interviews with BNOC and BP executives.

[108] Interviews with BNOC executives; Peter Rodgers, *The Sunday Times*, 21 May 1978, p.63; and House of Commons Nationalized Industries Select Committee (Sub-Committee B), 'Testimony by Frank Kearton, Chairman of BNOC,' Seventh Report, Reports and Accounts of Energy Industries, *British Parliamentary Papers*, 1977-78, Vol.XXXIX, p.43.

The production side of BNOC started off with the oil assets of the National Coal Board, and soon thereafter BNOC purchased 80 per cent of the Burmah Oil Company's North Sea oil fields.[109] The government also favoured BNOC by granting the company further substantial UKCS acreage in the fifth and sixth rounds (1976 and 1979). By 1982 BNOC had obtained production interests in nine North Sea oil fields and one gas field and was responsible for 7 per cent of all North Sea oil production.[110]

On the trading side, from the beginning BNOC activated the participation agreements with the oil companies giving it access to over 51 per cent of North Sea oil. This was unexpected by many; as one DEn civil servant explained:

> There were some ministers and certainly a lot of officials who thought BNOC would never in a million years think of exercising the options. They thought we would just have them there in case there was some crisis and then you could exercise the option... Whereas Kearton, backed by Tony Benn, was going to exercise the options right away and get in the oil industry and get some clout...Kearton is not just going to sit there and be a front man, he wanted a real job to do. At that time, ownership of oil, even if you paid market price for it, gave you clout. To have control of basically 50 per cent of UK oil was something.[111]

As another DEn civil servant simply stated: 'The oil companies were surprised. The oil companies were always surprised though.'[112] By 1981, with its own production, participation oil and royalty in kind, BNOC controlled up to 60 per cent of North Sea oil. Even after the production assets were sold in 1985, BNOC still

[109] Vickers and Yarrow, *Privatization: An Economic Analysis*, p.320; and Richard Bailey, 'Unequal Shares in the North Sea,' *Energy Policy*, December 1978, p.328.

[110] Webb, 'Energy Policy and the Privatization of the UK Energy Industries,' p.29.

[111] Interviews with Department of Energy civil servants.

[112] Interview with Department of Energy civil servant.

controlled 30 per cent of North Sea oil.[113] As one BNOC executive explained,

> by 1979, BNOC was the largest crude oil wholesaler, a very important source for non-Arab refineries. We were making decisions about where oil should go, on our own or with the government.[114]

Like many nationalized companies, BNOC soon found the government's financial control a severe constraint to expansion. The financial provisions for BNOC were established in the 1975 Oil and Pipelines Act. Through the National Oil Account (NOA) BNOC received funds for business transactions, but at the same time was obliged to submit, on a daily basis, all sums received. In June 1977, BNOC completed arrangements to raise $825 million through advance oil sales. This money was used to repay the loans from the National Loans Fund, thus significantly reducing BNOC's interest payments, and partly to finance new UKCS expansion. As one executive described it:

> The turning point for BNOC was when they convinced major bankers to loan us the $825 million, which was basically a forward sale of oil. Banks found BNOC had an entirely sensible business plan - went ahead and did the deal. The oil companies couldn't understand. The Banks played a role in persuading the oil companies to stop whingeing and go on with the game in town. The loan enabled BNOC to pay its own way, and not take away from money spent on hospitals etc, and helped to reduce the PSBR.[115]

In addition, BNOC expanded outside of the United Kingdom for the first time, in Dubai, Indonesia, the Republic of Ireland and France.[116]

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[113] Ian Hargreaves, 'Oil Supply Crisis Accord Would Not Stop Price Rises,' *Financial Times*, 15 July 1985, p.4; *Hansard Parliamentary Debates (Commons)*, 15 July 1985, col.80; Shelbourne, 'BNOC's Growth and Prospects,' p.6; and Webb, 'Energy Policy and the Privatization of the UK Energy Industries,' p.29.

[114] Interview with BNOC executive.

[115] Interview with BNOC executive.

[116] Britoil, *'Offer for Sale,'* by S.W. Warburg & Co and N.M. Rothschild & Sons on behalf of the Secretary of State for Energy, November 1982, p.6.

With so much oil under its control, BNOC grew into the position of being a price setter for North Sea oil. The price BNOC paid for its North Sea participation oil was set each quarter by BNOC with input from Energy and Treasury ministers.[117] Ultimately, however, BNOC was too small to be a world price leader. With the development of the spot market in the early 1980s and the drop in the price of oil in 1984, it became apparent that BNOC could at best only effect short-term prices.[118] One DEn civil servant explained, the government's aim was to smooth the jagged price fluctuations, and according to a BNOC executive, the government's instructions were to avoid short-term fluctuations.[119] The most serious costs of past crises have been those imposed by rapid and significant changes in the price of oil which have only been loosely linked to the scale of reductions in supply.[120] Thus, there were benefits to controlling the price, as explained in 1984 by the Minister of State for Energy Alick Buchanan-Smith:

> It is a small sum to pay in relation to the more general benefits and in relation to the higher cost to the economy which would be caused by the short term destabilization of prices.[121]

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[117] 'Grease the Oil-Prices Slide,' *Economist*, 5 January 1985; and *Hansard Parliamentary Debates (Commons)*, 18 December 1984, col.234.

[118] See the debate in *Hansard Parliamentary Debates (Commons)*, 18 December 1984.

[119] Interviews with Department of Energy civil servants and BNOC executive.

[120] Ian Smart, 'European Energy Security in Focus,' in Curt Gasteyger, ed., *The Future for European Energy Security* (London: Francis Pinter, 1985), p.157; 'Stocks for Crisis Management,' *Petroleum Economist*, October 1982, p.398; International Monetary Fund, *International Financial Statistics Yearbook*, 1990; BP, *Statistical Review of World Energy*, 1990; and Department of Energy, *Development of the Oil and Gas Resources*, 1990.

[121] *Hansard Parliamentary Debates (Commons)*, 18 December 1984, col.234.

BGC as a Player in the North Sea

The government also owned the British Gas Corporation (BGC) which evolved into an active player in oil exploration and production in the North Sea. The 1948 Gas Act nationalized over 1,000 town gas works and created the Gas Council. In the 1950s, the Gas Council was an ailing business and there was even talk of winding it down.[122] With the possibility of finding gas in the North Sea in the 1960s, however, the Council's prospects improved. Its functions were extended by the Gas Act of 1965 and the Council began to explore on and off-shore in order to gain some direct control of the primary resources on which they depended as well as to learn first hand the technology, the difficulties and the costs of exploration and development work.[123] Gas was discovered in 1966 and brought on-shore the following year. In 1968 the Council's first field became operational, and in 1969 it signed an industrial contract for the sale of gas to ICI. Under the Conservative government, the 1972 Gas Act consolidated the Gas Council into the British Gas Corporation (BGC), and in 1976 Denis Rooke became its chairman and a forceful defender of the corporation.[124]

While the Labour government never considered giving BGC the role of national oil company, the corporation was able to remain active in the oil industry

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[122] Interview with BGC executives; and Bill Jewers, 'We're Not As Different as Private Industry Thinks,' *Accountancy Age*, 23 June 1983.

[123] House of Commons Energy Select Committee,'Wytch Farm (Disposal of BGC Assets) Memorandum by British Gas Corporation,' First Report, Disposal of the British Gas Corporation's Interest in Wytch Farm Oilfield, *British Parliamentary Papers*, 1981-82, HC 138, p.ix; and Lynn Pearson, *Organization of the Energy Industry* (London: Macmillan, 1981), p.98.

[124] Interviews with BGC executives; and British Gas Corporation, *Annual Reports and Accounts*, 1980-85.

until 1982, building up a sizable portfolio which included interests in over 25 off-shore fields and the Wytch Farm on-shore field. The government had numerous opportunities to limit BGC's expansion into oil, but declined on each occasion. The first opportunity was when BNOC was created and the 1975 Petroleum and Pipelines Act specified that BNOC should receive the oil assets of the BGC.[125] BGC argued that it was impossible to know beforehand which fields were going to yield oil or gas, and in many cases they were found together. Others pointed out that some distinction could be made initially because gas fields were predominantly located in the south North Sea while oil is found in the north.[126] However, BGC's arguments predominated, as a BNOC manager explained: 'Rooke fought a rear guard action...He won the battle at the time because there was no one at BNOC yet to fight on the other side.'[127] A second opportunity occurred when BGC's petroleum production licence covering the Wytch Farm on-shore oil field came due in 1974. Instead of cancelling the contract, the DEn re-approved the license for a further forty years.[128] The Labour government, in fact, encouraged BGC's exploration and development by favouring applications for North Sea licenses where BGC was a partner.

Did Ownership Make a Difference in the 1979 Oil Crisis?

In 1979 Britain had the benefit of North Sea oil for the first time during a

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[125] Bailey, 'Unequal Shares in the North Sea,' pp.328-9; and *Hansard Parliamentary Debates (Commons)*, 13 March 1984, col.343.

[126] Interviews with BGC executives and Department of Energy civil servants.

[127] Interview with BNOC executive.

[128] House of Commons Energy Select Committee, 'Wytch Farm (Disposal of BGC Assets) Memorandum by British Gas Corporation,' p.xxiii.

world oil crisis. Although the world-wide supply disruptions in the spring of 1979 and then again in 1980 were not as great as during the 1973-74 crisis, the price of oil rose quickly. With North Sea supplies, Britain did not have to worry about serious shortages of oil. While the price increase was harmful to industry, it made high cost North Sea oil exploration more profitable, thereby increasing Treasury revenues.

The crisis, however, caused a relative scarcity of petrol during the summer of 1979. The irony of having North Sea oil production in full swing at the same time that apparent supply shortages were occurring at British garages was not lost on the British public, and caused Energy Secretary David Howell considerable political embarrassment.[129] Howell's emergency plan included taking North Sea oil royalties in kind rather than cash, increasing production incentives by suspending gas flaring restrictions, announcing a bigger licensing round, and ordering companies operating in the North Sea to cut exports from Britain - essentially using the participation agreements that the previous Labour government had enacted.[130]

These measures were not enough to abate the crisis. The problem was not a lack of oil, but the inability to shift supply destinations quickly because long-term supply contracts were the norm. Not even the state-owned BNOC could re-direct its short-term supply.[131] The disruptions soon stopped and the problem of short-term flexibility was solved, not by BNOC, but by competition between suppliers, the

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[129] Hann, 'The Process of Government and UK Oil Participation Policy,' p.258; and interview with Department of Energy civil servant.

[130] John Redwood, *Going for Broke...Gambling with Taxpayers' Money* (Oxford: Basil Blackwell, 1984), p.106.

[131] Interviews with BNOC executives; Roland Gribben, 'Oil Shortage Plans Revisited,' *Daily Telegraph*, 22 May 1979, p.6; and 'Howell Refuses to Impose Oil Controls,' *Daily Telegraph*, 6 June 1979, p.1.

development of a spot market in Rotterdam, and the subsequent shift from long-term to short-term contracts.[132] Thus, the increasing competitiveness of the oil industry, rather than BNOC and governmental directives, overcame the supply problem.

Conclusion

The two consistent factors in the government's involvement in the oil industry from 1914 to the mid-1980s were its investment in BP and its reliance on private international oil companies. Since the government agreed in May 1914 to become APOC's major shareholder, its role was limited to appointing two directors to the board and a veto power. Despite its holding in BP, the government relied primarily on private oil companies for supplies during World War I and World War II and to meet the increase in demand for oil in the post-war era, to develop the North Sea and to ensure oil supplies to Britain in a crisis.

Despite this consistency, there were many circumstances that changed. First, Britain's dependence on oil expanded from purely military needs to economic needs and became a vital input into the country's economy in the post World War II era. Second, the British government's ability to protect BP's interests in the Middle East decreased. And third, Britain's oil sources changed from foreign to domestic which radically affected the government's ability to influence the oil industry. With the discovery of oil in the North Sea and self-sufficiency by 1980, the government gained a new means of leverage over the oil industry.

To adapt to these changes, the British government created the Department of Energy in 1974 and the British National Oil Company in 1976 and allowed BGC to

[132] Yergin, *The Prize*, pp.718-9 and pp.767-8.

evolve into an active player in the North Sea. The DEn's primary means of controlling the oil industry were discretionary licenses and taxation. The DEn was also responsible for the offshore-supply industry, depletion policy and recording statistics. BNOC was a production company, the recipient of the government's participation oil and thus a major oil trader, as well as an advisory agent to the government. BGC with a monopoly over the British gas supply, also discovered, developed and produced oil in the North Sea. Ultimately, however, the government continued its reliance on the private oil companies for the development of the North Sea and for security of supply. The seven major oil companies, in fact, developed a majority of North Sea oil. Security was insured through participation agreements which gave the government the ability to control up to 51% of all production, and assurances which guaranteed that the private companies would supply in a crisis, provided they could charge the necessary price to cover any costs.

The sale of the government's oil assets ended one of the two consistent factors in the British government's long involvement in the oil industry, investment in BP. The sales, however, forced a continued reliance on the second, the private oil companies. In the next chapter I examine the specific details of how the government executed these sales, and then I turn to why.

Chapter Three: The Sequencing of the Oil Asset Sales in Britain

The sale of Britain's oil assets occurred during a ten year period, 1977-1987, and involved nine separate sales, with sizes ranging from just over £200 million for Wytch Farm to £5.5 billion for the last tranche of BP shares. The government received £8.5 billion in total for the sales, the biggest yield from any single industry sector in the privatization programme.[1] The costs of the privatization, are conservatively estimated at £224 million.[2] See summary in Table 3.1.

Though privatization is often described as a Conservative government phenomenon, the sales actually started in 1977 with the Labour government's sale of shares in British Petroleum. Starting here is crucial for a full understanding of the development of privatization in Britain. After reviewing the 1977 sale, I turn to the Conservative government's sales, which began with two more share sales of BP shares. In addition to BP, the government also sold the production operations of BNOC as Britoil and BGC's oil assets as Wytch Farm and Enterprise Oil. Britoil was sold in two tranches, 51% in 1982 and the remainder, except for one 'golden share,' in 1985. The golden share was only later redrawn after being tested in 1988 when Britoil was the subject of a takeover bid.

The government sold British Gas' on-shore oil field, Wytch Farm, and created Enterprise Oil with its off-shore oil fields and then sold the fields as a functioning entity. The sales were completed in 1987 when the government sold the remaining shares in BP. This last sale was complicated by the fact that not only was this sale

[1] Vickers and Yarrow, *Privatization: An Economic Analysis*, p.316.

[2] Costs were calculated using the average of existing estimates.

the biggest ever share offering at the time; it also coincided with the October 1987 stock market crash.

Because many of the details of these sales have not previously been recorded in scholarly works on privatization, although they are often listed as part of the government's privatization programme, much of the information in this explanatory chapter is based on first hand interviews. The review of these sales provides a useful prelude to the subsequent chapters.

Table 3.1. Proceeds and Costs from Oil Asset Sales

	Proceeds (£ millions)	Costs (£ millions)	Remaining Government Shareholding (%)
British Petroleum			68
June 1977	535	20	51
November 1979	290	9.6	46
July 1981	15	7	46
September 1983	565	9.4	31.5
October 1987	5,500	137.1	0
BNOC			100
November 1982	549	11.9	48.8
August 1985	450	15	0
British Gas' oil assets			
Wytch Farm May 1984	215	2.7	N.A.
Enterprise Oil June 1984	392	10	N.A.
Total:	8,511	223.7	0

3.1. British Petroleum - The First Sale

Although privatization as a phenomenon is commonly attributed to Margaret Thatcher, it was a Labour Cabinet which made the first major sale in 1977 by selling part of the government's holding in BP, reducing its stake in the company from 68 to 51 per cent. Pressure for the sale stemmed from the government's financial difficulties in the wake of the 1973 oil crisis and mid-1970s' global recession. The British government was twice forced to request a loan from the IMF, in November 1975 and in the summer of 1976, in order to fund a severe balance of payments deficit.[3] The IMF pressured the government to reduce its public sector borrowing requirement (PSBR), suggesting targets of between £6.5 and 7 billion for 1977-78 compared with the government's own estimate of £11.2 billion.[4]

The Chancellor Denis Healey lamented that the problem for all Cabinet members was that 'almost all of the spending cuts ran against the Labour Party's principles, and many also ran against ... campaign promises.'[5] The Cabinet was split over how to proceed, and selling BP shares provided a ready solution.[6] Joel Barnett, then the Chief Secretary of the Treasury, explained:

> If the money could be found elsewhere, all the better...it was much more sensible to raise £500 million [actually £535 million] in this non-

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[3] 'When Will Old Consoles Reach 50?' *Economist*, 6 December 1975, p.95; 'One Debt Repaid, the Next One Still Not Fixed,' *Economist*, 11 December 1976, p.119; and Margaret Garritsen de Vries, *The International Monetary Fund, 1972-1978: Cooperation on Trial. Vol.I Narrative and Analysis* (Washington, DC: International Monetary Fund, 1985), pp.464-8.

[4] de Vries, *The International Monetary Fund*, p.471; and Joel Barnett, *Inside the Treasury* (London: Andre Deutsch, 1982), p.102.

[5] Denis Healey, *The Time of My Life* (London: Michael Joseph, 1989), p.401.

[6] 'The Chancellor Proposes, the Cabinet Hopes it Disposes,' *Economist*, 4 December 1976, p.15; James Callaghan, *Time and Chance* (London: Collins, 1987), p.435; and Barnett, *Inside the Treasury*, p.104.

> deflationary way, rather than to have to cut the borrowing requirement with deflationary measures such as expenditure cuts or tax increases.[7]

Later, he explained: 'We couldn't worry about the future, it was the immediate cash advantage that was essential, even though in the long run the revenues might have been better.'[8] Even Tony Benn, the staunchest advocate of retaining the full shareholding, finally admitted that letting the sale go ahead was preferable to further spending cuts.[9]

Instead of counting this sale as revenue, the British government established the accounting practice of recording asset sales as negative expenditure. Due to the accounting procedure, the sales enabled the British government to lower the PSBR £535 million more than they might otherwise have done without further domestic spending cuts.[10] The decision to accept the accounting for the BP share sale as negative spending was not seen as very important; at the time no one foresaw the precedent that would be set. As one senior Treasury civil servant explained, it was a very pragmatic decision. The matter was discussed in the Treasury, and the solution adopted was based on the fact that the recently acquired BP shares from Burmah Oil were recorded as positive spending, and therefore the sale of BP shares should count as negative spending.[11]

The argument then became one of how much to sell and how much to cut.

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[7] Barnett, *Inside the Treasury*, p.108.

[8] Interview with Labour minister.

[9] Benn, *Against the Tide*, p.647 and p.653; and Tony Benn, *Conflict of Interest*,in Ruth Winstone, ed. (London: Hutchinson, 1990), p.102 and p.141.

[10] Interviews with Treasury civil servants and ministers. This aspect is further developed in Chapter Seven.

[11] Interview with Treasury civil servant and ministers.

Without much disagreement, the Cabinet decided to retain a 51 per cent holding, limiting potential charges from the left that they had relinquished control of a major state asset. Tony Benn was only minister who seemed to realize the political problems the choice might cause Labour later on. After the sale he wrote in his diary:

> We have handed some of the most valuable assets of this country to the Shah [The National Iranian Oil Corporation was reported to be trying to buy 1 per cent of BP shares] to the Americans and to private shareholders, and I am ashamed to be a member of the Cabinet that has done this...We have provided a blueprint for selling off public assets in the future and we will have no argument against it. It is an outrage.[12]

The logistics of the sale were complicated, however, by legal action from the Burmah Oil shareholders against the Bank of England. Although their claim was weak, the government had to proceed with the possibility that they could lose the suit. As a result they and could only sell the shares held by the Treasury, and not those of the Bank of England.[13]

Though the government did not consult BP before the announcement of the sale, they left BP to make the sale arrangements. Because it was at the time the biggest share sale ever, 25 per cent of the shares were offered in the United States in order to avoid flooding the British market. Expanding into the United States was also important to BP, who thought that it would reduce the United States government's resistance to BP's development plans in Alaska.[14] In late June 1977, 17 per cent of BP's shares, 66.8 million ordinary stock units of £1 each, were offered

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[12] Benn, *Conflict of Interest*, p.175.

[13] 'Crude Solution,' *Economist*, 11 December 1976, p.119; Benn, *Conflict of Interest*, p.75; and interview with BP executives.

[14] Interview with BP executives.

for sale at the price of 845p each. Because the offer was fully subscribed in Britain, the allocation to investors in the United States was in the end reduced from 25 per cent to 20 per cent. Preference was given to applications from occupational pension funds, BP employees and sub-underwriters. The government's holding was reduced to 51 per cent, of which 30.87 per cent was held by the Treasury and 20.13 per cent by the Bank. The sale raised £535 million for the Exchequer. The costs for underwriters and advisors, for this first sale, were estimated at £20 million.[15]

In 1979, a Conservative government led by Margaret Thatcher was elected, and soon began further sales of oil assets. As Chancellor Geoffrey Howe stated, 'the government was following the example set by the previous administration,'[16] by selling a 5.17 per cent tranche of BP stock in November 1979, which reduced the government's holding below the 50 per cent mark to 45.83 per cent. Just over 80 million shares of 25p each were sold in November 1979 at a price of 363p per share. The offer was again oversubscribed and considered a success, raising £290 million. The estimates for the costs of the sale ranged from the government's estimate of £5.2 million to the Public Accounts Committee's (PAC's) estimate of £14 million.[17]

The government's holding was further diluted in August 1980 to 44.61 per

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[15] Fraser and Wilson, *Privatization*, pp.51-2.

[16] As quoted in Fraser and Wilson, *Privatization*, p.52; and interpreted by privatization scholars: George Yarrow, 'Privatization and Economic Performance in Britain,' Carnegie-Rochester Conference Series on Public Policy, 1989, p.309; Vickers and Yarrow, *Privatization: An Economic Analysis*, p.324; and Samuel Brittan, 'The Politics and Economics of Privatisation,' *Political Quarterly*, Vol.55, No.2, April/June 1984, p.109.

[17] C.P. Mayer and S.A. Meadowcroft, 'Selling Public Assets: Techniques and Financial Implications,' *Fiscal Studies*, Vol.6 No.4, 1985, p.48; and Trades Union Congress, *Stripping Our Assets: The City's Privatisation Killing* (London: Trades Union Congress, May 1985), p.19.

cent as the result of the purchase by BP of Selection Trust.[18] The government's holding was again reduced (to 39.04 per cent) in July 1981 when the government ministers opted not to subscribe to a BP rights issue. Instead, the government sold their entitlements to the 100 million shares to other shareholders at a 15p premium of 290p per share compared to the rights issue price of 275p. The sale overshadowed the British stock market for the month of July, and net proceeds for the government were £8 million; £15 million total for the sale minus BP's expenses of £7 million.[19]

None of these sales required legislation because they involved a publicly traded company so they were not seen as a major policy departure either by the public or by the politicians who later became privatization advocates.[20] BP receipts, though, were always included in what the Conservatives later referred to as their 'privatization programme.' This programme received an enormous boost in September 1983 when the government sold a further 130 million ordinary shares of 25p each of BP at a minimum tender price of 435p each. The sale was fully subscribed and raised £565 million, with a government estimate of £9.4 million for the costs.[21]

3.2. The Britoil Saga - 1982-1988

Upon entering office, the Conservative government carefully considered what

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[18] Fraser and Wilson, *Privatisation*, p.53.

[19] Fraser and Wilson, *Privatization*, pp.52-3; Ronald Pullen, 'BP's Rights Issue an Eleventh Hour Success,' *Times*, 17 July 1981, p.21; and 'Hope Grows for £600 million BP Issue,' *Times*, 14 July 1981, p.19.

[20] Nigel Lawson, *The View from No.11: Memoirs of a Tory Radical* (London: Bantam Press, 1992), p.200.

[21] Fraser and Wilson, *Privatization*, p.53; and Mayer and Meadowcroft, 'Selling Public Assets,' p.48; and TUC, *Stripping Our Assets*, p.19.

to do with BNOC, by gathering information and gauging public opinion. The chairman of BNOC, Frank Kearton, meanwhile, had made it clear that he wanted to retire as soon as possible. He was replaced by an interim chairman, Ron Utiger, because, according to BNOC executives, the government had not yet decided what its policy was going to be.[22] In May 1980, nine months later, Philip Shelbourne, a merchant banker from Samuel Montague who had been working on privatization ideas with the Department of Energy (DEn), was appointed the chairman of BNOC, marking the beginning of the government's change in policy towards BNOC. Given his background, the new direction for the company was obvious - privatization in one form or another.[23] In 1982, BNOC became the largest privatization yet undertaken in Britain.

The delay from the date of Shelbourne's appointment until the sale of the first tranche of Britoil occurred because privatization was not a clear choice. Other issues demanded the government's attention, including BNOC's special privileges, and other options were presented as alternatives such as the forward sale of oil, a bond issue or an investment trust.[24] As Sir Alistar Morton, then deputy chairman of BNOC explained:

> The 'granny bonds,' or certified certificate bonds would be sold through the post office. The post office called one day and said we can't do this, it will take us two years to train our staff. The Treasury never understood this option, and it wasn't much discussed...a second option was an investment trust which would be managed by BNOC in perpetuity, in which shares in the trust would be sold to investors and

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[22] Interview with BNOC executive; and Peter Hill and Richard Evans, 'Top Executive Resigns form BNOC,' *Times*, 31 May 1980, p.19.

[23] Interview with BNOC executives.

[24] Redwood, *Going for Broke*, pp.106-7; and interview with Sir Alistar Morton, 15 October 1993.

> pay dividends based on the income of the trust...I had very bad relations with Howell, and he never seemed to understand these proposals.[25]

Privatization of BNOC was first set back in 1980 when a bill submitted by the Secretary of State for Energy, David Howell, giving the government the authority to sell BNOC was not given Parliamentary time. The following year, the new Secretary of State for Energy, Nigel Lawson, was almost thwarted, as Howell had been, by the lack of legislative time. Lawson had prepared two privatization bills, one for BNOC and one for BGC's oil fields, but the Cabinet ruled that there was time only for one. Instead of choosing one or the other, Lawson combined both measures into a single bill.[26] While the combination of the two bills meant presentational changes, it did not effect the timing or the outcome of either of the privatizations.

The question then became how to sell BNOC. The BNOC board, management and even Shelbourne opposed splitting the company, which entailed selling the production portion and retaining the trading operations in government ownership. They argued that a whole company would be stronger, provided balance to the majors in the North Sea, and offered better value for the shareholders.[27] One board member who strongly advocated keeping the company whole was Sir Denis Rooke, chairman of BGC, whose primary concern was the precedent such a split might create for the future treatment of BGC's gas operations.[28]

Yet no one persuasively suggested how the government could regulate a

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[25] Interview with Sir Alistar Morton, 15 October 1993.

[26] Webb, 'Energy Policy,' p.33; Lawson, *The View from No.11*, p.212; and interview with Department of Energy civil servant.

[27] Interview with Sir Philip Shelbourne, 18 October 1991.

[28] Interview with Sir Philip Shelbourne, 18 October 1991; and BGC executive.

private company trading state oil. Though there were plans for this function to be leased out to BNOC, they were not well developed.[29] Thus, as one BNOC executive summed it up:

> BNOC had been through the difficult times, had begun to gain the grudging respect of the industry, was making a lot of money, had shown we could be useful, and had reconciled our different roles. We were just beginning to gain an identity. To be faced with going private was exciting and scary, but to be faced with splitting was very sad. But I think if we were honest, we had to realize that it was quite difficult to put it [the trading side] in the hands of a private entity. So, in objecting to the split, in some senses we were objecting to privatization.[30]

Another reason the government wanted to retain the trading portion was to counter criticisms that it was relinquishing control of an important national asset.[31] In the end, Shelbourne convinced the board members that the government was the majority shareholder and it could do with the company what it wanted. Only three BNOC board members remained opposed, two trade unionists and Sir Denis Rooke.[32] BNOC was thus split; the production operations became Britoil and the trading operations remained BNOC.

Lawson agreed a minimum tender price with the consultation of Dundas Hamilton, a stockbroker whose firm had no connection with the issue, who was appointed the government's independent adviser on pricing. This was the first time the government had used an independent adviser. Nigel Lawson explained:

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[29] Interview with BNOC executive.

[30] Interview with BNOC executive.

[31] William Keegan, *Mr.Lawson's Gamble* (London: Hodder & Stoughton, 1989), p.96; Baker and Daniel, 'BNOC and Privatisation,' p.153; and Hann, 'The Process of Government,' pp.258-9.

[32] Interview with Sir Philip Shelbourne, 18 October 1991.

> It was, quite simply, designed to provide an extra line of defence against a possible investigation by the parliamentary watchdog, the Public Accounts Committee (PAC), the most powerful of all the Select Committees, which was by this time becoming restive at the apparent underpricing of privatization issues and consequent loss to the taxpayer.[33]

The government also responded to concerns over the future of Britoil - that it remain British and independent - by creating a special share, which became known as a 'golden share.' In a letter to the chairman of Britoil, Nigel Lawson stated that the government might

> wish in the relevant circumstances to use its voting rights of the Special Share to ensure that control of the Company remained in the hands of an independent Board of Directors.[34]

This sentiment was reinforced both in the Britoil prospectus and in Britoil's Articles of Association.[35]

The government then sold 51 per cent of Britoil in a share offering on 19 November 1982. The share price was expensive for BNOC's high debt/equity ratio compared to other large oil companies, and because the new corporation was unable to retain either the £219 million of profits or the £127 million remaining in the National Oil Account. Foreshadowing the events of the BP share offering five years later, the sale resulted in near disaster, as a sudden collapse in the price of oil just before the sale made Britoil even less attractive to investors. In addition, the sale was limited to Britain and was not offered in the largest stock market, the United

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[33] Lawson, *The View from No.11*, p.220.

[34] Britoil, 'Offer for Sale,' pp.16-7.

[35] Britoil, 'Offer for Sale,' p.16; Britoil Articles of Association, section (a) as printed in the Britoil, 'Offer for Sale,' pp.60-61.

States.[36] Of the 255 million shares of 10p each on offer at a price of 219p, only 69.7 million were taken up (27 per cent of the shares put up for sale), mostly by private investors and Britoil employees. The underwriters were forced to take up the remaining 73 per cent or 185.3 million shares. Because it was underwritten, the government received its guaranteed £549 million. The cost estimates ranged from £17 million by the National Audit Office (NAO) to £12.5 by the Public Accounts Committee and £11.3 million by the government.[37]

The under-subscription of the Britoil offer served as a good lesson in many respects. First, it made the Public Accounts Committee realize that underwriting served an important purpose, and was not just a way to give money to friends in the City as Labour claimed; and second, it demonstrated that an independent price adviser was helpful in deferring blame for an under-subscribed sale.[38] In fact, both practices were repeated in subsequent privatizations.

The government sold its remaining 48.8 per cent interest in Britoil in August 1985, and retained only its golden share. In comparison with the first issue, the 1985 sale was straightforward and was oversubscribed. Shelbourne described it as simply 'marvellous'.[39] The government reserved a portion of the 243 million shares at a price of 185p for the markets in the United States, Canada and Europe, but the

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[36] Britoil, 'Offer for Sale,' p.71.

[37] Max Wilkinson and Richard Tomking, 'Out of the Valley of Death But Only Just,' *Financial Times*, 31 October 1987, p.6; Martin Quinlan, 'Britoil Sale To Go Ahead,' *Petroleum Economist*, November 1982, p.449; 'City Shuns Britoil Offer,' *Petroleum Economist*, December 1982, p.510; Fraser and Wilson, *Privatization*, pp.28-9; Mayer and Meadowcroft, 'Selling Public Assets,' p.48; and TUC, *Stripping Our Assets*, pp.22-3.

[38] Lawson, *The View from No.11*, p.221.

[39] Interview with Sir Philip Shelbourne, 18 October 1991.

majority (over 40 per cent) was sold to British institutional investors. The government's gross proceeds were £450 million, and the *Financial Times* estimated the costs at £15 million.[40]

While Britoil proved it could survive on its own, BNOC could not. Because the government continued to insist that the company operate on the basis of long-term contracts in an effort to achieve the unstated policy of stabilizing oil prices, BNOC was forced to sell on the spot market at a loss. With the decline in oil prices in 1984 and 1985 this practice quickly became both expensive and politically embarrassing. As one Treasury civil servant complained:

> It is obviously very painful for the Treasury to have a body in the public sector buying oil at $28.65 and selling at a lower price; it gives us very great pain, be assured of that.[41]

From the point of view of BNOC, the government made too much over these losses because the price set by BNOC was the price the government used as a tax reference point, the higher BNOC's price in a declining market, the less the government lost in terms of revenues. In fact, three-fourths of the losses were gained back through taxes which were based on (this higher) price of oil. A BNOC executive explained:

> the sums involved were small compared to the total size, £12 million out of billions per year traded. BNOC had always made a small profit. It must have been embarrassing though for politicians to ask Parliament for money to cover the losses.[42]

The costs were magnified because BNOC was required under the 1982 Oil and Gas (Enterprise) Act to submit a Supplementary Estimate to Parliament for funds to

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[40] Interview with Sir Philip Shelbourne, 18 October 1991; Mayer and Meadowcroft, 'Selling Public Assets,' p.48; and Fraser and Wilson, *Privatization*, pp.29-30.

[41] As quoted in Yergin, *The Prize*, p.746.

[42] Interview with BNOC executive; also see 'Doubts About State Ownership - Editorial,' *Petroleum Economist*, September 1985, p.311.

cover any losses. The losses in 1984 meant the company had to submit a Supplementary Estimate, which led to an urgent enquiry by the House of Commons Select Committee on Energy. As conditions worsened, BNOC lost more money and had to repeat the process again later that year, thus making the loss of money a public embarrassment to the government.[43]

Because there was no saleable entity, legislation was introduced in March 1985 to abolish BNOC and replace it with a regulatory agency which would retain three of BNOC's functions:

- custody of participation agreements,
- disposal of oil received as royalty in kind, and
- management of the government's pipeline system.[44]

The government's reasons were summarized by then Minister of State for Energy Alick Buchanan-Smith:

> We have made changes because circumstances have changed. The situation is not the same as it was in the early 1970s, either in relation to the oil market or to the structure of the oil industry. The Bill is a reflection of the changes. What might have been appropriate 10 years ago is not necessarily appropriate today.[45]

The Oil and Pipelines Bill was enacted on 30 October, and BNOC was formally dissolved in March 1986. It was replaced by the Oil and Pipelines Agency (OPA),

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[43] Total losses for 1984 were £11 million. Lord Croham, Chairman of BNOC, 'Chairman's Statement,' *Annual Report and Accounts*, 1984, p.3-4; interview with BNOC executive; 'Government Pricing Role Under Review,' *Petroleum Economist*, January 1985, p.24; 'Abolition of BNOC,' *Petroleum Economist*, April 1985, p.114; and *Hansard Parliamentary Debates (Commons)*, 18 December 1984, 13 March 1985, 14 May 1985, 15 July 1985.

[44] Vickers and Yarrow, *Privatization: An Economic Analysis*, pp.321-2.

[45] *Hansard Parliamentary Debates (Commons)*, 15 July 1985, vol.83, col.87.

newly created within the DEn.[46]

The story of Britoil and BNOC did not end in 1985. The government's one remaining tie to Britoil, its golden share, again ensnared the government in the company's affairs in late 1987 when BP initiated a takeover bid for Britoil. The government's position fluctuated throughout. Prime Minister Margaret Thatcher initially stated: 'I understand that it is a commercial transaction, and it is not for us to interfere.'[47] Complicating matters, however, it was revealed a few days later that Atlantic Richfield (Arco) had also begun acquiring stock in an effort to take over Britoil. The government reversed its position on the 18th of December 1987, with a statement from the Treasury confirming that the government would use its golden share to prevent a takeover of Britoil.[48]

Ministers did not reveal how they would use the golden share, if at all, even to the Britoil management. Thus neither Britoil nor the bidders knew whether or how the government would prevent a transaction.[49] From the accounts given by Britoil executives, it appears that Arco was intimidated by the golden share while BP was not, which explains why Arco agreed to sell its shares in Britoil to BP in January 1988. Then, with over 50 per cent of Britoil's shares, BP made an offer for the outstanding shares at 500p per share. As Britoil chairman Philip Shelbourne pointed out, this offer was attractive to Britoil shareholders as many had bought their shares

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[46] Fraser and Wilson, *Privatization*, p.31.

[47] *Hansard Parliamentary Debates (Commons)*, 10 December 1987, vol.124, col.582.

[48] *Hansard Parliamentary Debates (Commons)*, 16 December 1987, vol.124, col.1107, and 11 January 1988, vol.125, col.13-6,73; and Fraser and Wilson, *Privatization*, p.30.

[49] Interviews with Britoil and BNOC executives; and Britoil, 'Reject BP's Inadequate and Unwelcome Offer,' 28 January 1988, p.10.

in the first issue at a price of 218p per share. In fact, the Britoil share price had never risen above its issue price until the takeover bid.[50]

According to some accounts, BP had acquired as much as 80 per cent of the Britoil stock. With such a high acceptance rate by the shareholders, the government had little choice but to allow the sale to proceed.[51] On the 23 February 1988, the Chancellor announced that the government would not use its veto power in exchange for certain assurances from BP regarding employment, exploration and development of Britoil's assets, Britoil's Glasgow base, and the composition of the Britoil board.[52]

3.3. The Sale of British Gas' Oil Assets

The government faced its toughest opposition from BGC. Like BP, BGC was a large well-established company with the advantage of having a natural monopoly on gas. BGC had the benefit of having a strong and politically well connected chairman, Denis Rooke, who was determined to maintain BGC's operations intact. Not surprisingly, therefore, the BGC sales were different from the others. The government's tactic was to strip away oil assets, leaving BGC's gas-related organization and staff intact. The on-shore oil assets of Wytch Farm were sold to another company in a trade sale, while the off-shore assets were transformed into a new company, Enterprise Oil, and sold in a tender offer. Together, the sale of these

[50] Interview with Sir Philip Shelbourne, 18 October 1991.

[51] Interview with Sir Philip Shelbourne, 18 October 1991.

[52] Fraser and Wilson, *Privatization*, p.30; and *Hansard Parliamentary Debates (Commons)*, 8 February 1988, vol.127 col.34; and 23 February 1988, vol.128, col. 149-60.

assets accounted for roughly 10 per cent of total British oil production.[53] To minimize Rooke's power, Lawson appointed three new board members. He recalled: 'These three eminent businessmen could not be pushed around by anyone. They also kept me better informed than my officials were usually able to do.'[54]

Wytch Farm

The management delayed the sale of Wytch Farm for two years and seven months after the issue of the first directive, and it was in fact the longest of all privatizations to be completed. The first oil asset sale did not need new legislation as the field under consideration, Wytch Farm, was an on-shore oil field and was covered under the 1972 Gas Act. The Act allowed the Secretary of State to direct the corporation 'to dispose of any part of their undertaking or of any assets held by them.'[55] As with the BP sale, it was left to BGC to make the arrangements for the disposal. BGC invited tenders in July 1982. The management of BGC argued against the sale publicly and privately and was unhelpful in the government's efforts to gain information and slow to act on decisions. BGC estimated that Wytch Farm was worth £450 million, while Wood Mackenzie and Company, a stockbroker firm, gave an independent valuation of £165.5 million. The bids received reflected Wood Mackenzie's estimate and did not exceed £160 million. BGC nevertheless argued that

[53] Webb, 'Energy Policy,' p.33.

[54] Lawson, *The View from No.11*, p.214.

[55] Gas Act 1972, Section 7.(2)(a); British Gas Corporation, *Annual Report and Accounts*, 1981-82, p.18; *Hansard Parliamentary Debates (Commons)*, 13 March 1984, vol.56, col.354.

a great loss would occur if the assets were sold so cheaply.[56]

They also argued that the government's directive was a punishment for success. Since BGC discovered Wytch Farm itself, and because it was one of their most successful finds, they could not perceive legislative reasons why the government was forcing them to sell one of their most significant achievements.[57] They argued that the sale would harm the national interest; specifically, the sale would damage BGC's standing as a free partner in exploration and development for hydrocarbons; it would endanger BGC's ability to bring a sufficient level of expertise and knowledge to the negotiation of gas contracts; it would cost the taxpayers money because a forced sale was unlikely to realise the full value of the assets; and it would threaten environmental disruption as the buyer would not necessarily have the same high level of commitment to solving environmental problems as BGC.[58]

Despite BGC's protests, Secretary of State for Energy, Nigel Lawson, told BGC in March 1983 that it would be commercially justifiable and in the national interest to proceed.[59] BGC was ordered to sell its 50 per cent share in Wytch Farm to the Dorset Group, a consortium of five independent British companies. Due to complications, the sale did not go through until over a year later, in May 1984. The Group agreed to pay £85 million up front, and an additional £130 million when

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[56] *Hansard Parliamentary Debates (Commons)*, 13 March 1984, vol.56, col.340, col.344-6 and col.355; House of Commons Energy Select Committee, 'Wytch Farm (Disposal of BGC Assets) Memorandum by British Gas Corporation,' p.v and p.xxvii.

[57] Jewers, 'We're Not As Different as Private Industry Thinks'; and James Erlichman, 'British Gas Exceeds Targets,' *Guardian*, 10 June 1983.

[58] House of Commons Energy Select Committee, 'Wytch Farm (Disposal of BGC Assets) Memorandum by British Gas Corporation,' p.xxi-xxii.

[59] *Hansard Parliamentary Debates (Commons)*, 13 March 1984, vol.56, col.346.

production reached 20,000 b/d (production was then under 4,500 b/d, but was predicted to reach 40,000 b/d.)[60] The government's costs for the sale were £98,388, but the cost to BGC was about £1.75 million, which was met out of the proceeds of the sale.[61]

Enterprise Oil

Like with Wytch Farm, BGC was opposed to the sale of their off-shore oil assets. Their biggest complaint was the loss of revenue without compensation. In the 1984 *Annual Report and Accounts*, the company complained that the sale had 'an adverse effect on its [BGC's] financial position which will continue to be felt into the future.'[62] At the same time, however, BGC was earning huge profits by this time which the government was having difficulty getting out of the corporation.[63]

Some of the problems the government faced in the Wytch Farm sale were meant to be overcome by the specific legislation in the 1982 Oil and Gas (Enterprise) Act which gave the Secretary of State for Energy clear authority to sell BGC's off-shore oil assets, Enterprise Oil. While the idea of a straight trade sale was initially considered, the option was rejected for three reasons.[64] First, based on the

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[60] 'Wytch Farm Sale Finalised,' *Petroleum Economist*, June 1984, p.232.

[61] TUC, *Stripping Our Assets*, p.13; and *Hansard Parliamentary Debates (Commons)*, 8 June 1984, vol.61, col.306.

[62] BGC, *Annual Report and Accounts*, 1984, p.5.

[63] BGC, *Annual Reports and Accounts*, 1982-88; and interviews with Treasury civil servant and BGC executive.

[64] Dominic Lawson, 'The Management Page: Enterprise Oil - Built from the Top Down,' *Financial Times*, 18 June 1984, p.10; 'The Lex Column: A Test for Free Enterprise,' *Financial Times*, 28 June 1984, p.48; 'A Setback for Privatisation,' *Financial Times*, 29 June 1984, p.22; and interview with Department of Energy civil servant.

assumption that the private bidder would have been an American company, the government feared a political reaction to a transfer of oil assets overseas.[65] Second, the DEn saw the opportunity to create an independent British oil company.[66] And third, tax benefits afforded by the operations' oil exploration activities would accrue to the purchaser and would have reduced the Treasury's net gain.[67] Therefore, though several international companies approached the government to buy the blocks, they were turned down.[68]

A directive from the Secretary of State for Energy in August 1982 required BGC to dispose of its interests in five UKCS Blocks. These blocks were incorporated on 26 November 1982 under the name British Gas North Sea Oil Holdings Limited, and started trading on 1 May 1983, while remaining a subsidiary of BGC. In September 1983, all the directors of British Gas North Sea Oil Holdings Limited resigned, and ownership was transferred to the Secretary of State, without compensation to BGC. The name was changed to Enterprise Oil Limited, and two managers, one from the DEn, were appointed to run the company and create an infrastructure. In late October 1983, a second batch of BGC oil assets, interests in 20 UKCS Blocks, were incorporated under the name British Gas North Sea Oil Exploration Acreage Limited. On 20 December 1983, these assets were acquired by Enterprise Oil but remained under the control of the Secretary of State for Energy, again without compensation to BGC. Enterprise was re-registered as a public

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[65] Interview with Department of Energy civil servant; and Peter Riddell, 'UK News: Whitehall Unshaken by Criticism of Enterprise Oil Sale,' *Financial Times*, 5 July 1984, p.6.

[66] Interview with Department of Energy civil servant.

[67] Interview with Department of Energy civil servant.

[68] Interviews with Department of Energy civil servant and business executive.

company in April 1984.[69]

As a privatization candidate and a new company, Enterprise Oil faced three risks. First, as pointed out in the prospectus, the 1983 Labour Party Conference had passed a resolution to re-nationalize Enterprise Oil.[70] Second, while the oil business in general was risky, Enterprise Oil was in particular handicapped by the mature stage of its fields which were set to decline after 1987, and could not guarantee new discoveries.[71] Thirdly, as a newly created company, Enterprise Oil had no track record.

These difficulties were addressed in a number of ways. The government made it clear that they would have no continuing involvement in Enterprise following the sale offer, except as the holder of the 'special share'. In all other respects the government confirmed that Enterprise Oil would be treated in the same way as any other private sector oil company.[72] The new team set out a business strategy for Enterprise Oil which took into consideration Enterprise's mature asset base. To give further credibility to the company, the government agreed to contribute the earnings from the fields since they began trading as an entity in May 1983, giving the

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[69] Enterprise Oil, 'Offer for Sale,' by Kleinwort Benson Limited on behalf of the Secretary of State for Energy, September 1984, p.1 and p.19; British Gas Company, *Annual Report and Accounts*, 1984, p.5; and BGC, *Annual Report and Accounts*, 1982-83, p.5; Ray Dafter, 'UK News: Enterprise Oil packaged for Sale,' *Financial Times*, 26 October 1983, p.10; and Enterprise Oil, *Annual Report and Accounts*, 1984, p.8.

[70] Enterprise Oil, 'Offer for Sale,' p.2; also interpreted and reported by the *Financial Times* as a potential risk; and 'The Lex Column: Reward Before Enterprise,' *Financial Times*, 20 June 1984, p.21.

[71] Enterprise Oil, 'Offer for Sale,' p.35.

[72] Enterprise Oil, 'Offer for Sale,' p.2.

company a significant cash resourcing, £70 million, with which to proceed.[73] Lastly, although the company did not have a history, the government had been able to attract some qualified oil professionals with individual track records who in turn were able to set up a respected team. Enterprise did not have much trouble finding qualified personnel. Recent takeover victims such as Gulf and Getty provided a large pool from which to choose.[74] At the end of 1983 there were only 8 employees; in June 1984 there were 48, and by the end of 1984 there were 90 staff.[75] Having agreed to the government's objectives, given up their previous jobs and put their names on the prospectus, the management as well as the government had a stake in the success of Enterprise Oil as an independent entity.[76]

In the end another measure was added, a special share, to ensure the continued independence of Enterprise for a limited period. The share was held by the Secretary of State for Energy and was scheduled to be redeemed on 31 December 1988. With this special share, the government had the ability to out-vote all shareholders in the event any person sought to exercise or to control the exercise of more than 50 per cent of the voting shares.[77] The Enterprise management saw the special share as a necessary protection for an immature company. In order to give the government's

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[73] Enterprise Oil, 'Offer for Sale,' pp.2-3; Dominic Lawson, 'The Management Page: Enterprise Oil - Built from the Top Down,' *Financial Times*, 18 June 1984, p.10; and Ian Hargreaves, 'UK News: Enterprise Oil Sizes Up Takeover Targets,' *Financial Times*, 13 December 1983, p.8.

[74] Interviews with Department of Energy civil servants.

[75] Interview with Department of Energy civil servant; and Enterprise Oil, 'Offer for Sale,' p.12.

[76] Interview with Department of Energy civil servant.

[77] Enterprise Oil, 'Offer for Sale,' p.2 and p.43.

policy of creating a new independent oil company the chance to work, the company needed some breathing space from predators.[78]

Although nine paragraphs were devoted to the provisions of the Special share, the circumstances in which it would be used were not clear. In fact, the government's intentions were stated more clearly in the *Financial Times*:

> the only circumstances where the government would exercise its Golden Share powers would be if undesirable interests declared their intention of taking control. A straightforward build-up of shares in the company would not be legitimate grounds for government intervention.[79]

The proposed sale was well received by the City; the consensus was that Enterprise was worth the £520 million being tendered. By addressing the problems, spelling out the details in the prospectus and starting a promotional campaign, the new Enterprise Oil team overcame the potential price discounting sometimes encountered in the flotation of new companies.[80] The issue was offered only in the United Kingdom, as the government was again sensitive to nationalistic feeling towards the North Sea. Enterprise, on the other hand, saw limiting the sale to Britain as a way of gaining favour with lenders in the City who they were sure to need in the future as the company required funds. There was, therefore, no company push to expand the offering to Europe or the United States.[81]

The entire shareholding in Enterprise Oil was sold on 27 June 1984; until then

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[78] Interviews with Department of Energy civil servants.

[79] Ian Hargreaves, 'UK News: Takeover Protection for Enterprise Oil Until 1988,' *Financial Times*, 14 June 1984, p.8.

[80] Peter Riddell, 'UK News: Whitehall Unshaken by Criticism of Enterprise Oil Sale,' *Financial Times*, 5 July 1984, p.6.

[81] Interview with Department of Energy civil servant; Enterprise Oil, 'Offer for Sale.'

sales of on-going companies had always carried out in parts. Though the government had addressed many difficulties, it could not control the inherent fluctuations in the oil industry. In this case, the collapse of the spot market price for crude oil two days before the offering pushed the short-term value of the stock down. There was some discussion of delaying the issue, but there were too many forces moving the issue to the set date, including buyers having the funds available, the timeliness of the prospectus and the government's privatization timetable. Since the issue had been underwritten, Enterprise was guaranteed to be sold and the government was guaranteed its money. Only the underwriters stood to lose.[82] The government received its £392 million for the sale, while the cost estimates ranged from £9 million by the government to £11 million by the National Accounting Office (NAO).[83]

Though the Treasury received its money, there were many problems brought on by the decision to proceed with the sale. Due to the uncertainty in the oil market, investors were cautious and failed to fully subscribe the issue. Interested stock brokers waited to buy shares on the open market which was sure to be lower than the underwritten price. In fact, only 66 per cent of the shares were subscribed in the end. This provided a prime opportunity for a takeover bid, and just hours before the bidding closed, Rio Tinto Zinc (RTZ, the British based international mining and industrial group) subscribed to 49 per cent of the shares.[84]

The dilemma for the government was whether to support the principles of free

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[82] Interviews with Department of Energy civil servants.

[83] Fraser and Wilson, *Privatization*, p.34; 'The Blackballing of RTZ,' *Economist*, 7 July 1984, p.16; Mayer and Meadowcroft, 'Selling Public Assets,' p.48; TUC, *Stripping Our Assets*, p.25.

[84] Interview with Department of Energy civil servant; Fraser and Wilson, *Privatization*, p.34.

enterprise or to support the strategy of creating an independent British oil company. RTZ had sought only 49 per cent of the shares for fear of invoking the government's special share, though 50 per cent had not been identified as a trigger.[85] Alistar Frame, the chairman of RTZ, personally informed the Secretary of State for Energy, Peter Walker, of his company's intentions that day. As a major mining company, Frame decided that it was not worth ruining RTZ's relationship with the government with the takeover of Enterprise Oil.[86] According to the Enterprise Oil management, Walker was furious anyway. Walker believed that government intentions were sacred. He was determined that Enterprise should remain an independent company, with the full concordance of Enterprise Oil's executives.[87]

On June 28th, Walker announced that in keeping with the government's objective to make Enterprise Oil an independent British oil company, no bidder would be allotted more than 10 per cent of the shares in the offer. The City underwriters were thus left with 73 per cent of the 210 million Enterprise shares.[88] RTZ tried yet again with a dawn raid on 2 July 1984, when trading began for Enterprise Oil shares on the London Stock Exchange and acquired another 5 per cent. Free trading in the market and little investor interest in the shares meant that by July 1984 RTZ was able to acquire 29.9 per cent of the shares (the maximum allowed by law) on the open market for 1p above the original offer price. Yet because of the government's golden

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[85] 'A Setback for Privatisation,' *Financial Times*, 29 June 1984, p.22.

[86] Interview with business executive.

[87] Interview with Department of Energy civil servant.

[88] Peter Riddell, Dominic Lawson and Stefan Wagstyl, 'Government Limit on RTZ's Enterprise Stake Angers City,' *Financial Times*, 29 June 1984.

share, RTZ lacked full control.[89]

The government's efforts to intervene in the market while simultaneously affirming its belief in free market operations made it look inept. There was a strong case that RTZ, a well-managed international company, would be an ideal vehicle for expanding Britain's presence in the world oil industry.[90] The oil assets of RTZ were estimated to be only one third the size of those of Enterprise. Even with the combined assets, the RTZ oil company would not have been a dominant force in the North Sea compared to the majors.[91] Enterprise, however, would have been controlled by a corporation larger than BGC with international interests, and thus a mere transfer of assets from one large corporation to another could have occurred. A takeover by RTZ was not acceptable to a government determined to have an independent British oil company - even if that was not what the free market offered. With the government preventing any further acquisition of Enterprise shares, RTZ decided in December 1985 to transfer its holdings in Enterprise Oil to London and Scottish Marine Oil (LASMO) in exchange for a 25 per cent holding in LASMO.[92]

3.4. The Government's Final BP Sale

Though BP was not always considered a nationalized industry and therefore not truly part of the government's privatization programme, it proved useful to the

[89] Peter J. Curwen, *Public Enterprise: A Modern Approach* (London: Harvester Wheatsheaf, 1986), pp.184-5; and 'The Blackballing of RTZ,' *Economist*, 7 July 1984, p.16.

[90] 'A Setback for Privatisation,' *Financial Times*, 29 June 1984, p.22.

[91] Dominic Lawson, 'RTZ Bids to Lift Enterprise Oil Stake to 29.9%,' *Financial Times*, 3 July 1984, p.1.

[92] Fraser and Wilson, *Privatization*, p.34.

government in that context again in 1987. As Nigel Lawson explained:

> The postponement of the water flotation in July 1986 had created a gap in the privatization timetable, and I had announced in March 1987 that it would be replaced with the sale of the government's remaining 31.5 per cent shareholding in BP.[93]

The last BP sale was publicly described as part of the government's policy to sell its minority shareholdings in companies as and when circumstances permitted.[94] The government offered BP a golden share, but was turned down, leaving BP as one of the few privatized companies without one.[95]

On the crest of a booming stock market, the government decided to sell all of its remaining shares, against the advice of BP, who argued that three tranches would be more sensible, especially as the company needed to raise more capital themselves through a share issue. One BP executive explained:

> We didn't believe the market had the capacity easily to accept all those shares. I don't think even they [ministers] would have tried to do it except that we had such a raging boom. BP shares were up to 440p. We would have much preferred three tranches. We decided to offer a new issue, and ride the back of the government. We needed to do a rights issue; it was just tactics that we did it with the government. The banking advice at the time was if you want to do it, you need to wrap it all up and package it together. So we had to shift, being faced with a dead 'no' from the Lady - she was going to sell the whole lot. Then, if they believe they can sell, and the bankers believe it, why not get our rights issue too.[96]

The combined shares made the £7 billion issue the largest ever attempted in the

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[93] Lawson, *The View from No.11*, p.757.

[94] *Hansard Parliamentary Debates (Commons)*, 18 March 1987, vol.112, col.1011; Peter Riddell and Max Wilkinson, 'Government to Sell BP Stake,' *Financial Times*, 19 March 1987, p.1.

[95] Cosmo Graham and Tony Prosser, 'Golden Shares: Industrial Policy By Stealth?' *Public Law*, Autumn 1988, p.429.

[96] Interview with BP executive.

London market.[97]

Another early point of conflict between BP and the government over the sale was over the sale's geographical allocation of shares. BP's strategic plan included geographical diversification of share ownership, with the goal of having 10 per cent of the shares held outside Britain by the end of 1987. In contrast, the government's policy objective was to maximize British equity ownership. The government also realized that the inclusion of the United States market would ensure the largest return for the Exchequer; and in the end the government allocated over 24 per cent to the United States market, 8 per cent to Japan, and 5 per cent each to Canada and Europe.[98]

The government sold 2,194 million BP shares in October 1987. Of these, 1,850 million were the government's remaining 31% stake in the company and the remaining 459 million were new share issues by BP. On 15 October, the government announced the fixed price of 330p per share, (to be paid in three instalments, the first being 120p), which was just before the October stock market crash. Between the 14th and 27th of October, the *Financial Times* ordinary share index fell by 28 per cent, and the BP share price dropped 26 per cent, from 351p to 259p. The final date for applications for the government's offer was 28 October at which point only 70 million shares were applied for, 3 per cent of the total. Because the issue was underwritten, the government again received its full £5.5 billion; and because the government had

[97] Lucy Kellaway, Philip Stephens and Max Wilkinson, 'BP Seeks £1.5 Billion In Offer Linked to Privatisation,' *Financial Times*, 22 July 1987, p.1; and *Hansard Parliamentary Debates (Commons)*, 21 July 1987, and 21-9 October 1987; Fraser and Wilson, *Privatization*, pp.53-5.

[98] 'The Lex Column: BP / Comment on Plans to Internationalise Shareholder Base,' *Financial Times*, 30 January 1987, p.36.

bought BP's new issue shares outright, BP itself received £1.5 billion. The £114 million fee to the underwriters, though large, was worthwhile in this case as virtually all (97 per cent) of the shares were held by underwriters: 1,179 million shares in Britain, 506 million shares in the United States, 160 million shares in Japan and 105 million shares each in Canada and Europe. The £23.1 million spent on advertising, however, had virtually no effect in the wake of the market crash.[99]

The decision to sell shares in the United States caused an unforeseen problem. Underwriters in the United States do not normally spread the risk of an issue to sub-underwriters, so for the BP issue four American underwriters bore the whole of the disaster themselves. The Americans, therefore, were understandably the ones who put the most pressure on the British government to withdraw the issue.[100] Bending to pressure from the underwriters, the government finally agreed via the Bank of England to provide a floor price of 70p for the partly paid shares (compared to the partly paid flotation price of 120p per share.) The Bank only had to buy back 38 million shares because the Kuwait Investment Office (KIO) purchased most of the outstanding BP shares at a few pence above the floor price. By November 1987 KIO had accumulated a 10 per cent stake in BP (nearly 600 million shares), but the KIO gave the government assurances that it was buying the shares only as an investment, and that it had no ambitions to control BP. By May 1988, though, KIO's stake had

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[99] Fraser and Wilson, *Privatization*, pp.53-5; *Hansard Parliamentary Debates (Commons)*, 21 July 1987, and 21-9 October 1987; Clive Wolman, 'Underwriting Change for State Industry Flotations,' *Financial Times*, 8 September 1988, p.6; Gareth David, 'City Floats Toward £1 Billion Sell-off Fees,' *Sunday Times*, 4 December 1988; and Maurice Samuelson, 'Share Advertising Cost £23 Million,' *Financial Times*, 22 January 1988, p.7.

[100] Max Wilkinson and Richard Tomking, 'Out of the Valley of Death But Only Just,' *Financial Times*, 31 October 1987, p.6.

risen to 22 per cent of BP shares.[101]

The government faced a difficult problem: Should it allow the free-market to work or should it interfere and prevent a foreign entity from buying and controlling Britain's largest oil company? Instead of legislating, the government chose a less public route of referring the issue to the Monopolies and Mergers Commission (MMC).[102] On October 4, 1988 the MMC ordered KIO to reduce its holdings in BP from 21.69 per cent to 9.9 per cent. Kuwait responded with threats of retaliation against the British government both financially and diplomatically, and also against British individuals, banks and companies. The Kuwait government stated that it would 'take all necessary steps to protect Kuwait's economic interests in Britain.' Kuwait had investments of $85 billion (£50 billion) overseas, and one fifth of that was in Britain.[103]

BP was particularly concerned over how KIO would dispose of the shares. Although the British government extended the deadline for the reduction from one year to three, there was still a fear that KIO would dump the shares on the market or worse, sell them to another company who might then vie for a takeover.[104] In

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[101] Ivan Owen, 'Parliament and Politics, Kinnock in Clash Over BP Holdings,' *Financial Times*, 20 November 1987; Fraser and Wilson, *Privatization*, pp.55-6; and *Hansard Parliamentary Debates (Commons)*, 27-9 October 1987, 3-26 November 1987, 12-26 January 1988, 5-8 February, 4-20 May 1988, 27 October 1988, 7 December 1988, and 1 February 1989.

[102] Interview with BP executive.

[103] Christopher Walker, 'Kuwaiti Press Hits at BP Stake Order,' *Financial Times*, 7 October 1988, p.25; and 'Kuwait "Astonished" over BP' *Financial Times*, 10 October 1988, p.25.

[104] 'Two Extra Years for KIO to Cut BP Stake,' *Financial Times*, 17 December 1988, p.17; and Max Wilkinson and Richard Jones, 'Kuwait Defies British Government By Lifting BP Stake Above 20%,' *Financial Times*, 12 March 1988, p.1.

January 1989, when KIO proposed a buy-back formula, BP was eager to accept. The government was kept informed, but was not a party to these negotiations. Nonetheless, in the final agreement, the government made a substantial contribution: BP agreed to buy back KIO's 11.7 per cent stake for £1.95 billion, and the government provided a refund of £458 million to KIO on Advance Corporation Tax payable on the sale of shares. KIO received 305p per share, 50p above the current BP share price, and made 16p per share profit at a time when other share holders were still suffering a loss from the 1987 sale.[105]

The sale was a boost to BP's independence, one of the BP management's primary objectives. Its chairman, Sir Peter Walters, told shareholders that the purchase of KIO's shares would remove any fears amongst potential investors that BP could have been influenced by a major shareholder which was also a member of OPEC.[106] Once through this crisis, the BP management sought to distance itself again from the British government and present itself as a truly international company.[107]

Conclusion

This chapter set out the specifics of how the British government sold its majority holding in BP, Britoil, Wytch Farm and Enterprise Oil in the space of 10 years, raising £8.5 billion against a minimum cost of £224 million. As the oil assets

[105] 'Big Kuwait Profit From BP Shares', *Financial Times*, 4 January 1989, p.1; and 'BP Pays Kuwait £1.95 Billion for Stake,' *Financial Times*, 4 January 1989, p.19.

[106] 'Shareholders Support BP Buy Back,' *Financial Times*, 1 February 1989, p.25.

[107] 'BP to Give Investors Details of Revamp,' *Financial Times*, 30 January 1989, p.21.

were some of the government's first privatizations, the process was a learning one, particularly regarding the extent to which the nationalized industry management would oppose the sales, the importance of safeguards such as independent pricing and underwriting, and the uncertainty of the markets. In the next four chapters, I examine the underlying reasons why the government sold these oil assets.

Chapter Four: Constraints and Opportunities Presented by the International System

Aggregate power-structure models developed by realists emphasize the importance of states' interests and argue that these interests are determined by the state's position in the international system. From these interests, the models predict the general behaviour of states.[1] These models, however, are too crude to predict specific domestic policy decisions. To predict more particular national policies, some scholars have developed models that disaggregate by issues. For example, David Lake in *Power, Protection and Free Trade* argues that: 'by examining the international economic structure, the position of a country within it, and the changes in the structure over time, it is possible to explain and predict trade strategies.'[2] Rather than using the realists' premise that the state is a homogeneous rational actor with definable interests and seeing policy outcomes as the direct result of a state's position in the international system, I view the state as a complex entity composed of individuals and institutions, and the state's position as one that determines a set of parameters to policy decisions. From this perspective, international factors determine only a range of policy options available to politicians. A strong position increases the

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[1] Robert Keohane, 'Theory of World Politics,' in Robert Keohane, ed., *Neorealism and Its Critics* (New York: Columbia University Press, 1986), pp.180-9; Waltz, *The Theory of International Politics*; and Joseph Grieco, 'Anarchy and the Limits of Cooperation: A Realist Critique of the Newest Liberal Institutionalism,' *International Organization*, Vol.42, No.3, Summer 1988.

[2] Lake, *Power, Protection and Free Trade*, pp.29-40; also see Charles Kindleberger, 'Dominance and Leadership in the International Economy: Exploitation, Public Goods and Free Rides, *International Studies Quarterly*, Vol.25, June 1981, pp.249-51; Robert Gilpin, *U.S. Power and the Multinational Corporation: The Political Economy of Foreign Direct Investment* (New York: Basic Books, 1975) p.22; and Stephen D. Krasner, 'State Power and the Structure of International Trade,' *World Politics*, Vol. 28, April 1976, p.323.

options available to policy makers, while a weak position limits the alternatives politicians can feasibly pursue. Other intervening variables narrow that range in a way that cannot be predicted from international variables alone.

Borrowing from the aggregate and disaggregate models, I develop a two variable construct to illustrate this view of the international system (see Figure 4.1.).

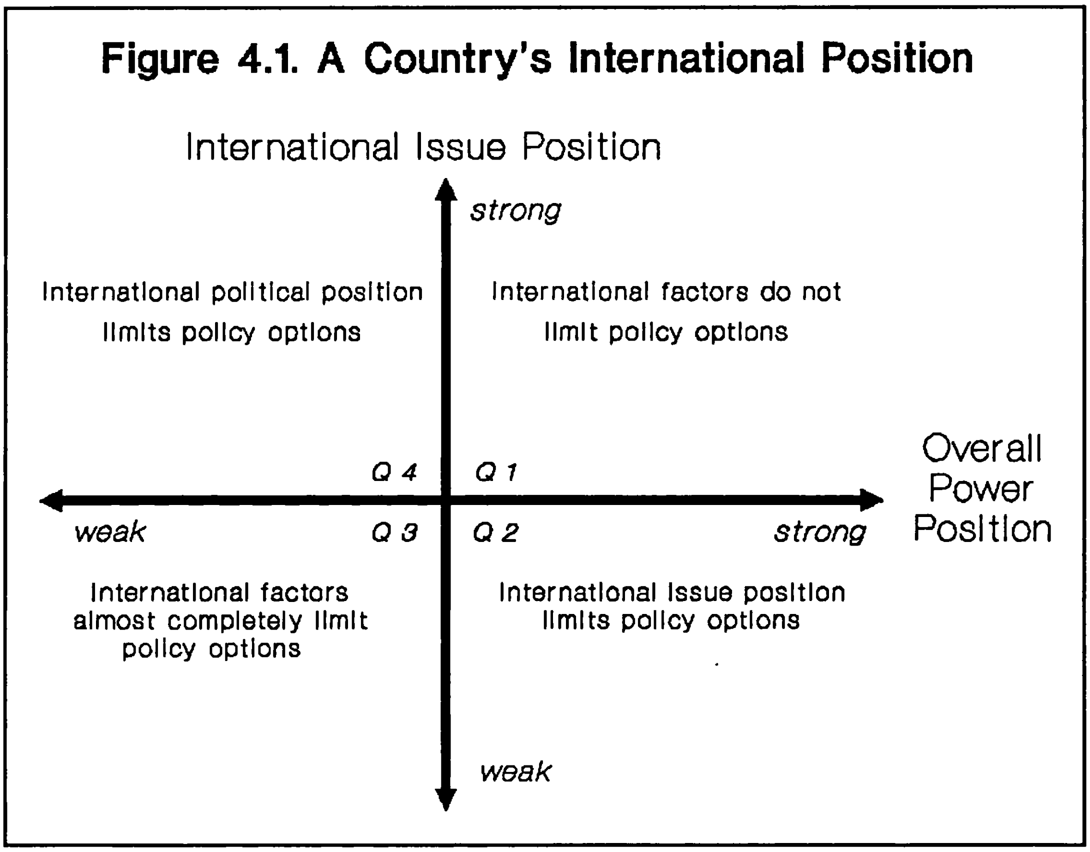

Figure 4.1.

The first variable, a country's overall power position, is an aggregate variable which measures the state's overall power in the international arena. Though there are many definitions for power, in this case I use Susan Strange's meaning where a state's power is determined by its ability to set the agenda and design international rules and customs. It includes four aspects of control: security, production, credit and knowledge.[3] These can be operationalized using indexes of country's military expenditure, GNP per capita, allocation of IMF Special Drawing Rights (SDRs), and rate of literacy. In these graphs I use measures for 1978.[4]

The second dimension, a sector specific economic variable, measures a country's position in a specific issue area. The key factor which determines a state's international issue position is the state's position in that sector relative to other countries.[5] For oil, I suggest this can be measured by the country's level of production as a percentage of world total.[6] For finance, I propose this can be measured as the sum of a country's total reserves and central government revenue.[7]

The stronger the country is in terms of the specific economic issue and the more powerful the state, the more options are available to the state's policy makers and the less susceptible they are to international forces.[8] In this case, domestic factors play a greater role in determining outcomes (quadrant 1). Conversely, the weaker the state's position, the fewer policy options are available and the more its

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[3] Susan Strange, *States and Markets*, pp.25-7. The definition of power is highly contentious issue as there are many aspects, including short term and long term power as well as structural and relational power. Strange's definition is meant to be used as a first approximation.

[4] Charles Lewis Taylor and David Jodice, *World Handbook of Political and Social Indicators, Volume 1*, Third Edition (London: Yale University Press, 1983), Tables 1.6, 3.6, C-39 and 5.3.

[5] Robert Keohane and Joseph Nye, *Power and Interdependence: World Politics in Transition*, (Cambridge, MA: Harvard University Press, 1979); and Lake, *Power, Protection and Free Trade*, pp.29-30.

[6] BP, *Statistical Review of World Energy, 1990.*

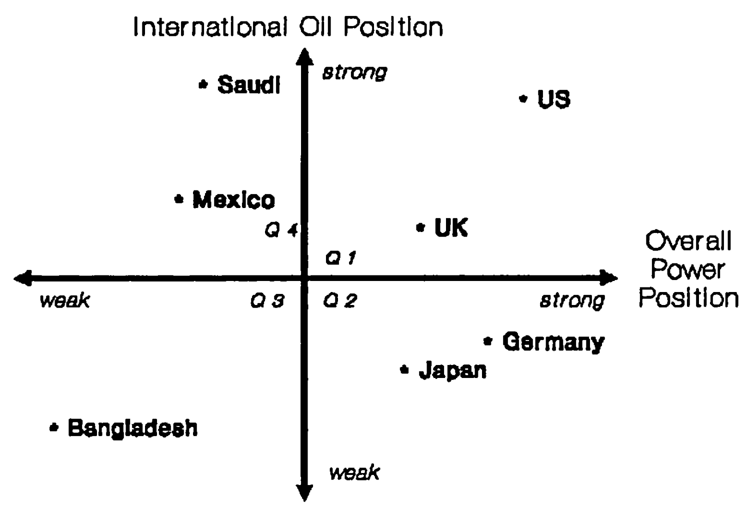
[7] International Monetary Fund, *International Financial Statistics Yearbook* (Washington, DC: IMF, 1986).

[8] Edward Morse, *Modernization and Transformation of International Relations* as discussed in Gourevitch, 'The Second Image Reversed,' p.892.

policy makers are constrained by international factors (quadrant 3). When a state's position is weak either in overall power or on a specific economic issue, the policy options available are limited unless the strength of the state's stronger position compensates to provide additional options or alternatives (quadrants 2 and 4). Inevitably, economic and political issues are linked and reinforce each other, and OPEC serves as one such example of this. It is important to note, then, that Figure 4.1 is used only as an analytical framework.

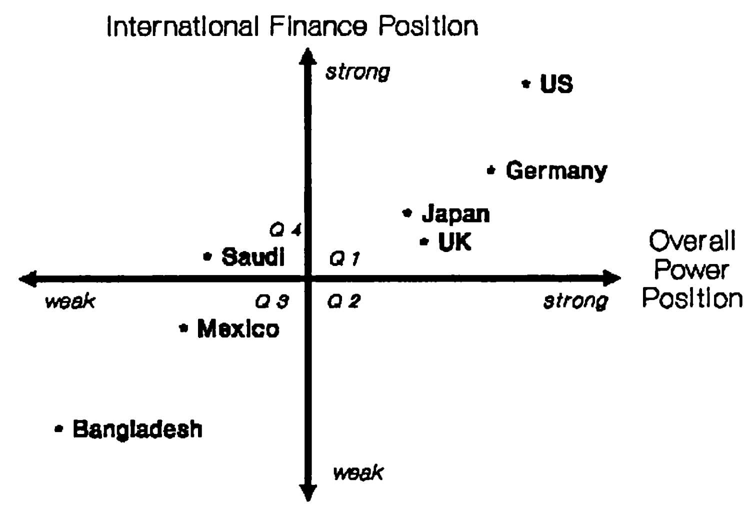
Examples for specific issues and countries from 1976 and 1980 help to illustrate the relative strengths and weaknesses of different countries' positions. On the issue of oil, Britain's position was strong in 1980 because its own oil production was increasing and would soon surpass domestic consumption. With its substantial overall power position, Britain was well placed in terms of sovereignty over its oil policy (quadrant 1). Britain's options were limited only by the countries with a stronger international position, in this example, the United States. Saudi Arabia was also in a strong oil position as the world's largest oil producer, but was not as strong overall power position as Britain (quadrant 2). Conversely, Germany had more overall power, but, as a major oil consumer with no domestic supplies, was weaker in terms of oil and

Figure 4.2. A Country's International Oil Position



had few options in terms of oil policy and fewer means to influence other countries (quadrant 2). Mexico, Japan and Bangladesh were all weaker, both in overall power and in terms of oil than Britain and therefore were virtually unable to influence Britain's oil policy.

Figure 4.3. A Country's International Finance Position



Turning to the international financial issue, due to severe balance of payments problems Britain's finance position in 1976 was not as strong as its international oil position (see Figure 4.3). Britain's overall power position remained the same but, its international finance position had deteriorated so that Britain was barely remained in quadrant 1.[9] British policy makers were therefore more limited in their policy options in terms of finance than oil. This difference is obvious when the positions of the world's strongest financial countries are compared. Because of their strong position, Germany and the United States were the most able to influence British government policy decisions, with possibly some influence coming from Japan which was in a stronger financial situation but slightly weaker overall power position. Saudi Arabia, Mexico and

[9] Because this label may raise the broader image of Britain as the home to one of the world's financial capitals, the City of London, it is important to note that the definition of financial position here refers only to the government's reserves and revenues, not the size of the country's private financial industry.

Bangladesh were not influences due to their relatively much weaker positions (quadrants 3 and 4).

From this view, we would expect the international financial situation and the structure of the oil industry to have affected British politician's decision to sell their country's oil assets. One of the major criticism of realists (and neo-realists) is that the importance of international organizations is not taken into account. Neo-liberals argue that international organizations and regimes play a substantial role in shaping the international system and states' options.[10] Incorporating this view, I also explore the extent membership in international organizations influenced the British government's decision to sell its oil assets.

4.1. International Financial Pressure on Britain

The importance of the world economy on domestic policy making is generally recognized. Andrew Gamble stresses its impact on Britain in the late 1970s and 1980s:

> Of overriding importance in shaping domestic policy in recent years have been events in the world economy. From this perspective there have been so far two crucial phases in the life of the Thatcher government, determined by the slump in the world economy between 1979 and 1982, and then by the recovery between 1982 and 1987.[11]

Other scholars confirm the importance of the world economic situation on British policy making in this period,[12] as did the civil servants and politicians I

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[10] Stephen Krasner, ed., *International Regimes* (Ithaca, NY: Cornell University Press, 1985).

[11] Andrew Gamble, *The Free Economy and the Strong State: The Politics of Thatcherism* (London: Macmillan Education, 1988), p.98.

[12] Keith Middlemas, *Power, Competition and the State: Vol.3, End of the Postwar Era: Britain Since 1974* (London: Macmillan, 1991) p.6, pp.241-2 and pp.273-4.

interviewed.[13] The world recession was such an all encompassing factor, though, that it is difficult to determine whether it was the primary cause of different outcomes such as privatization. In general, it is agreed that the world recession was a contributing factor to countries' deficits by increasing demands for public spending, as well as decreasing government tax revenue. This background pressure was one of the reasons why privatization emerged on national agendas throughout the world.[14] Its specific effect was apparent on Britain's financial situation and the ensuing IMF crisis in 1976-77. As one Treasury civil servant stated: the impetus for the BP sales 'really started with the 1973-74 recession followed by the 1974-75 Labour spending.'[15]

The civil servants and politicians that I interviewed agreed that the government would not have sold a 17 per cent shareholding in BP in 1977 if the IMF had not imposed strict conditions on its loan to Britain in 1976.[16] So it is important to understand why the IMF became involved, why the IMF focused on the Public Sector Borrowing Requirement (PSBR) and, critically, why an asset sale was accepted as negative spending. The details of the 1976 IMF crisis in Britain have been well

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[13] Interview with Treasury civil servant; also see Lawson, *The View from No.11*, p.34, pp.89-93 and p.245.

[14] Jeffrey Henig, Chris Hamnett and Harvey Feigenbaum, 'The Politics of Privatization: A Comparative Perspective,' *Governance: An International Journal of Policy Administration*, Vol.1, No.4, October 1988, pp.445-7.

[15] Interview with Treasury civil servant.

[16] Interviews with Department of Energy and Treasury civil servants; and Nick Gardner, *Decade of Discontent, The Changing British Economy Since 1973* (Oxford: Basil Blackwell, 1987), p.91.

documented elsewhere,[17] although I draw on first hand interviews to supplement these analyses.

Britain was forced to go to the IMF after experiencing large and successive balance of payments deficits and failing to repay a six month loan to the Bank for International Settlements (BIS, the central bank of Central Banks). Both the BIS and the IMF were heavily influenced by their largest donors, the United States and Germany, who felt that Britain's economic problems were deeper than a temporary insufficient cash flow. They therefore wanted the 'excesses and lack of scruples' corrected and structured the IMF agreements to achieve that end.[18] While it is generally accepted that Britain had no alternative to the IMF loan, many, including Prime Minister James Callaghan, initially thought that the government could persuade the IMF through its leading members to lessen the severity of the conditions imposed. Callaghan was initially bolstered by gestures of support from Germany and the United States, but ultimately, both gave their full backing to the IMF plan.[19]

The United States and the other industrialized countries had a self-interest in

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[17] Kathleen Burk and Alec Cairncross, *'Goodbye Great Britain,' The 1976 IMF Crisis* (London: Yale University Press, 1992); Kendall W. Stiles, *Negotiating Debt, The IMF Lending Process* (Oxford: Westview Press, 1991); and de Vries, *The International Monetary Fund.* As well as individuals' accounts: Barnett, *Inside the Treasury*; Benn, *Conflict of Interest* and *Against the Tide*; Barbara Castle, *The Castle Diaries 1974-76* (London: Weidenfeld & Nicolson, 1989); Edmund Dell, *A Hard Pounding: Politics and Economic Crisis 1974-76* (Oxford: Oxford University Press, 1991); Healey, *The Time of My Life*; Leo Pliatsky, *Getting and Spending: Public Expenditure, Employment and Inflation* (Oxford: Basil Blackwell, 1984); and Bernard Donoughue, *Prime Minister, The Conduct of Policy Under Harold Wilson and James Callaghan* (London: Jonathan Cape Ltd, 1987).

[18] Middlemas, *Power, Competition and the State*, pp.151-4; and Stiles, *Negotiating Debt*, pp.140-1.

[19] Burk and Cairncross, *'Goodbye Great Britain,'* p.62, p.80, p.111 and p.115; Middlemas, *Power, Competition and the State*, p.154; 'The Chancellor Proposes, the Cabinet Hopes it Disposes...But Markets Will Decide,' *Economist*, 4 December 1976, p.16; and Stiles, *Negotiating Debt*, p.130.

their concern for Britain's policies. There was a high degree of interdependence linking the welfare of Britain with the other industrialized countries. These links were embodied in institutions such as the North Atlantic Treaty Organization (NATO) and the European Community (EC). The international role of sterling meant that a currency collapse would cause great financial instability which in turn could have been harmful to all the industrialized (and British Commonwealth) economies.[20] The importance to the international community of improving Britain's creditworthiness is therefore understandable, as is the pressure coming from those countries and organizations most able to influence Britain.

What is not as obvious, however, is why the level of the PSBR was seen as a crucial target in financial markets and the IMF boardroom when the actual problem was the balance of payments. The way that the PSBR dominated all other targets in discussions is illustrated in the letter of intent from Chancellor Denis Healey to the IMF, in which he refers to the PSBR in eleven out of twenty-five paragraphs. The next most discussed economic factor, mentioned in seven paragraphs, was public spending, a target closely related to the PSBR.[21] Civil servants in the Treasury suggest that the PSBR was not a dominant policy variable until the IMF intervened in 1976.[22]

Why then did the IMF demand attention to the PSBR target? In part the answer lies in the practicalities of Britain's situation, and in part in the IMF's

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[20] Stiles, *Negotiating Debt*, pp.143-44.

[21] Denis Healey, Letter of Intent, as printed in Burk and Cairncross, *'Goodbye Great Britain,'* Appendix, p.229.

[22] Interviews with Treasury civil servants.

monetarist approach. The common financial market and international political view of Britain's economic problems was that they were the result of inflation and continued deficit spending. Britain's public spending was growing faster than in any other European country, and the rate of inflation was the highest in Europe, except for Italy.[23] Britain's creditors became reluctant to lend in sterling for fear that the value of their loans would depreciate due to inflation.[24] The excessive spending of the British government was obvious to the IMF team in 1976. The accounts of the crisis convey direct approaches and solutions; no one mentioned formal theory or doctrinaire solutions.[25] Thus, the focus on the size of the PSBR can be justified as a visible indicator of the government's economic problems.

One problem with the interpretation that the IMF saw the PSBR as the cause of Britain's problems is that it does not explain why the IMF allowed countries to adopt 'easy' measures to decrease the PSBR. Jacques Polak of the IMF defines easy measures as those that are not durable or have widely varying effects on the growth of the economy and the fiscal situation in the medium term.[26] In addition to the sale of BP shares to offset spending, there are three other examples of the British government choosing easy measures. First, the government altered the financing of the nationalized industries, for example by raising British Gas' prices and reducing

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[23] OECD statistics quoted in Burk and Cairncross, *'Goodbye Great Britain,'* pp.223-4.

[24] Donoughue, *Prime Minister*, p.66.

[25] De Vries, *The International Monetary Fund*; Healey, *The Time of My Life*, p.412; Callaghan, *Time and Chance*, p.419 and p.436; Barnett, *Inside the Treasury*, pp.97-111; Dell, *A Hard Pounding*, pp.248-272; Bernard Donoughue, 'The Conduct of Economic Policy, 1974-79,' in Anthony King, ed., *The British Prime Minister*, Second Edition (London: Macmillan, 1985), p.66; and interview with Treasury civil servant.

[26] Jacques Polak, 'The Changing Nature of IMF Conditionality,' Essays in International Finance, No. 184, Princeton University, Princeton, NJ, September 1991, p.39.

the company's capital expenditure by £100 million. Second, the capital expenditure for BNOC was excluded from the public expenditure totals because they were a 'special case' according to the Secretary of State.[27] Third, the Treasury made three major changes in the definition of public expenditure in 1977 which reduced the ratio of public expenditure to Gross Domestic Product (GDP) in 1975-76 from 60 per cent to 46 per cent.[28]

The IMF officials' emphasis on the PSBR target may be better explained by their belief in monetarism which emphasizes achieving targets rather than how they are achieved. The IMF and most of the international financial community turned to monetary policy when the United States abandoned the gold standard in 1971 which caused the global system of fixed exchange rates to deteriorate, giving governments more discretion over monetary policy. Because monetary policy works primarily through exchange rates and current accounts, it tends to become the more powerful instrument for demand management in a free float system.[29]

The IMF was particularly receptive to the use of monetary policy because it had found that in many countries monetary data had proved the most accurate and most readily available of all economic data.[30] The evidence from other cases of IMF intervention suggests that the IMF did indeed emphasize this visible indicator in

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[27] Interviews with BGC executives; and Pliatsky, *Getting and Spending*, p.146.

[28] Peter Browning, *The Treasury and Economic Policy 1964-1985* (London: Longman, 1986), pp.232-3.

[29] N.F.R.Crafts and N.W.C.Woodward, 'Introduction and Overview,' in N.F.R.Crafts and N.W.C.Woodward, eds., *The British Economy Since 1945* (Oxford: Clarendon Press, 1991), p.14; Michael Burda and Charles Wyplosz, *Macroeconomics, A European Text* (Oxford: Oxford University Press, 1993), p.219 and pp.223-4; and Burk and Cairncross, *'Good-bye Great Britain,'* p.143.

[30] Polak, 'The Changing Nature of IMF Conditionality,' p.34.

general. In a survey of 105 IMF programs from 1969 to 1978, nearly four-fifths included specific clauses in the agreements to limit the national government's borrowing, mostly by limiting their use of bank credit. Even the countries without specific clauses made policy statements citing their intentions, all of which included deficit levels and deficit financing targets.[31] The IMF has consistently focused on borrowing as a means of control across countries since 1969. In addition, in previous cases of IMF intervention in Britain, controlling public spending was always emphasized.[32]

Because monetary policy was accepted in the markets, there was an aspect of a self-fulfilling prophecy in reaching an agreement with the IMF using monetary targets. If world financial markets believed that the British economy was stronger by achieving certain targets, creditors would be more willing to lend to the government and the immediate balance of payments crisis would be solved. The IMF itself acknowledges the impact of its 'seal of approval.'[33] This is in fact what happened in Britain's case: once the IMF loan and conditions were put in place, there was a quick restoration of the pound's value. The ease with which Britain attracted foreign

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[31] Only a few of the clauses though incorporated specific targets for the government's budget deficit or borrowing requirement. The survey did not include the 1976 British case. W.A. Beveridge and Margaret Kelly, 'Fiscal Content of Financial Programs Supported by Stand-By Arrangements in the Upper Credit Tranches, 1969-78,' IMF Staff Papers, Vol.27, No.2, June 1980, pp.220-1.

[32] See letters of intent from the Chancellor of the Exchequer to the Managing Director of the IMF: 23 November 1967, para 10, and measures announced 18 November 1967; 22 June 1969, para 5, 6 and 7. As quoted in Susan Strange, International Monetary Relations as Vol.2 of Andrew Shonfield, ed., *International Economic Relations of the Western World, 1959-1971* (Oxford: Oxford University Press, 1976), pp.166-172.

[33] Polak, 'The Changing Nature of IMF Conditionality,' p.22.

exchange in 1977 indicates that much of the original problem was one of perception.[34]

It was IMF policy to let governments decide how specific targets should be met.[35] When the Cabinet decided to sell a portion of its BP shares, the Treasury decided to treat the sale receipts not as revenue, but as negative public expenditure. (For further description of the Cabinet's deliberations, see Chapter Three.) Treasury ministers confirmed that the IMF did not query this accounting practice.[36] One Treasury civil servant pointed out that the IMF officials 'were the ones so concerned about the targets that they didn't have much room to argue.'[37] The IMF has since changed its practice of non-interference in the detail, Jacques Polak explains, because governments tend to choose easy remedies, the outcomes can be 'ineffective and indeed counterproductive.'[38] As the IMF became more supportive of privatization, it narrowed the range of acceptable accounting practices. Sale proceeds are now required to be considered as loan repayments, whereas previously asset sales could also be used to off-set spending.[39]

Taken in isolation, the 1977 sale of BP shares is neither complicated nor

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[34] Stiles, *Negotiating Debt*, p.142; and de Vries, *The International Monetary Fund*, p.463 and p.476.

[35] Beveridge and Kelly, 'Fiscal Content of Financial Programs,' p.205; Polak, 'The Changing Nature of IMF Conditionality,' p.39; Pliatsky, *Getting and Spending*, p.148; and interviews with Treasury civil servants.

[36] Interviews with Treasury civil servant and ministers.

[37] Interview with Treasury civil servant.

[38] Polak, 'The Changing Nature of IMF Conditionality,' p.39.

[39] International Monetary Fund, *Manual on Government Finance Statistics* (Washington, DC: International Monetary Fund, 1977 and 1986); and Ali Mansoor, 'Budgetary Impact of Privatization,' IMF Working Paper, 15 October 1987, p.2.

necessarily even very interesting. However, because the sale was successful in enabling the British government to meet its IMF agreed targets, it set an important precedent. The success was reinforced by the IMF as it became an advocate of privatization. Although the privatization concept was little used before 1983, from 1984 to 1990, privatization was a condition for an IMF loan in at least 15 countries.[40] While Britain did not have to return to the IMF for loans in the 1980s, credibility in the world economy remained important. Thus, the acceptability of privatization proceeds by the IMF as government revenues made it an attractive option in the future.

Why the 1976 crisis was the first to lead to privatization needs further examination. Britain experienced repeated sterling crises after WWII (1947, 1949, 1951, 1955, 1957, 1964, 1965, 1966, 1967, 1975 and 1976),[41] most stemming from balance of payments deficits, and yet the only sterling crisis that produced an asset sale was in 1976. Why did the 1976 crisis result in an asset sale when the others did not? Britain had owned BP since 1914, and it could have sold shares on any of the previous occasions. In fact, the government had an offer to sell AIOC during the period 1953-57 (see Chapter Two), which coincided with the sterling crises of 1955 and 1957, and yet government ministers at that time decided not to sell its shareholding. Britain's finance position can therefore explain why an asset sale in general became an attractive policy option but cannot explain why ministers selected

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[40] This number was compiled by a search on the Profile computer data base using the *Economist* and the *Financial Times*, searching for all articles containing IMF and privatization. This search revealed 15 different cases where privatization was part of the conditions for IMF loans; also see Chapman, *Selling the Family Silver*, p.7.

[41] Burk and Cairncross, *'Good-bye Great Britain,'* p.5.

the option at one opportunity and not another or why they chose to sell oil rather than other assets.

4.2. Britain's Changing International Oil Position

Though oil has been an international currency since the 1950s, if not earlier, much of the reason why oil was an attractive asset to sell in the late 1970s and 1980s is explained by the changes in the structure of the international oil industry, particularly the rise of OPEC, the discovery and development of new sources of oil, and the transition of the industry from control by an oligopoly to a market driven industry. Oil assets have in fact been a common choice for asset sales throughout the world, including France, Argentina, Malaysia and Portugal.[42]

The Changing Structure of the International Oil Industry

The history of the oil industry consists of three distinct eras. As these are broader and have different implications than the periods of British government intervention in the oil industry, they are important to review here briefly. The first, from 1900 into the 1960s, was the era of the oligopoly of private oil companies, the majors.[43] Second, during the 1960s and 1970s, was the era of the oligopoly of Middle East oil producing countries, OPEC. Though brief, this second era was

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[42] Alice Rawsthorn and David Buchan, 'French Left-Overs on the Block,' *Financial Times*, 27 May 1993, p.23; 'Financial Times Survey: Portuguese Industry,' *Financial Times*, 14 November 1983; John Barham, 'International Company News: Argentina Sells Energy Group in Three Units,' *Financial Times*, 12 July 1993, p.19; and Victor Mallet, 'Survey of Malaysia,' *Financial Times*, 28 August 1992, p.VI.

[43] The 'majors' or Seven Sisters as they were also known included Jersey (Exxon), Socony-Vacuum (Mobil), Standard of California (Chevron), Texaco, Gulf, Royal Dutch/Shell and BP. There was also an eighth sister, the French national oil company, CFP.

significant as the impetus for the transition from the first to the third era. And the third, the late 1970s to the present, is the era of the free market. I review each period briefly before considering the implications for the British government's ownership of oil assets.

Following the break up of the Standard Oil trust in 1911, the resulting American companies along with BP and Shell sought to control the oil industry through formal agreements signed in 1928 and 1934.[44] While the smaller oil companies looked upon the agreements as a conspiracy, the United States and British governments supported the arrangements.[45] The dominance of the major international oil companies held through the 1950s and 1960s. As shown in Figure 4.4., the majors owned 98.2 per cent of world crude oil production outside of the United States and the communist countries in 1950.

Control of the industry by a few large companies ensured sufficient supply was produced and was distributed evenly during crises. This was especially important during the two World Wars.[46] International oil sharing measures were necessary to ensure supplies to Britain and all the members of the wartime alliances. The inclusion of Standard Oil and Shell, however, were what really made the system work, and vast

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[44] Raymond Vernon, *Two Hungary Giants: the United States and Japan in the Quest for Oil and Ores* (Cambridge, MA: Harvard University Press, 1983), pp.20-1; Yergin, *The Prize*, p.204 and p.264; and McBeth, *British Oil Policy 1919-1939*, pp.76-7 and pp.106-7.

[45] Yergin, *The Prize*, p.260 and p.266; and McBeth, *British Oil Policy 1919-1939*, pp.76-7 and pp.106-11.

[46] Lesser, *Resources and Strategy*, p.43 and pp.78-91; McBeth, *British Oil Policy 1919-1939*, p.25; Anthony Eden, *Facing the Dictators* (London: Cassell, 1962), pp.287-97; Yergin, *The Prize*, pp.319-23 and pp.362-395; and Louis Turner, *Oil Companies in the International System* (London: The Royal Institute of International Affairs, 1978), p.39.

United States' supplies made it possible.[47]

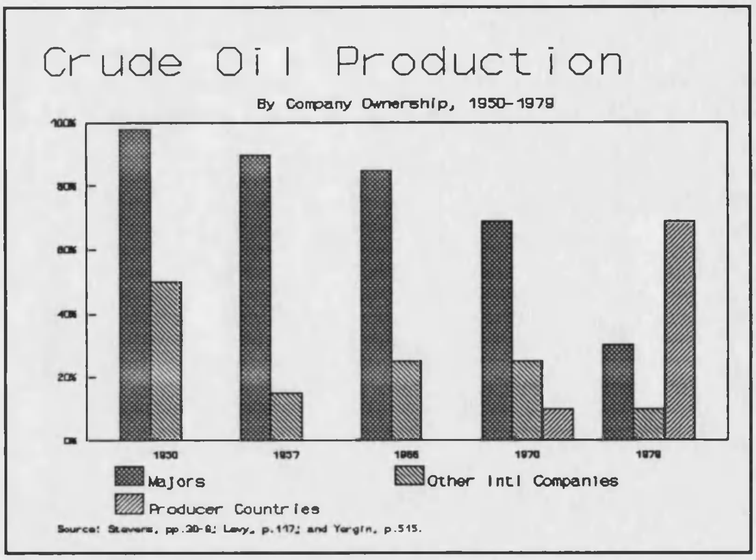

Figure 4.4.

The oil industry grew significantly after 1945 with the economic growth of the western economies and new oil discoveries in the Middle East. There was thus room to accommodate competition from the 300 private companies and 50 state-owned companies who either entered the international market or expanded their participation in it from 1953 to 1972.[48] The sheer size of the industry can be seen from the investment required in the post World War II period. From 1955 to 1970, the industry spent $100 billion in exploration and development of oil, and a further $115 billion to produce and distribute it.[49] The competition, including increased production from the Soviet Union, contributed to falling oil prices through the 1960s. But it also cut into the majors' control of world crude oil production which, by 1982, had fallen to less than 30 per cent of world crude production compared to 69 per cent

[47] The United States supplied 80% of the Allies wartime oil requirements, Yergin, *The Prize*, pp.177-78; and Ferrier, *The History of the British Petroleum Company*, pp.235-7.

[48] Neil H. Jacoby, *Multinational Oil: A Study in Industrial Dynamics* (London: Collier Macmillan, 1974), p.120; Yannis Stourharas, *Are Oil Price Movements Perverse!: A Critical Explanation of Oil Price Levels 1950-1985* (Oxford: Oxford Institute for Energy Studies, 1985), pp.11-5; Brian Levy, 'World Oil Marketing in Transition,' *International Organization*, Vol.36, No.1, Winter 1982, pp.116-9.

[49] Christopher Tugendhat and Adrian Hamilton, *Oil, the Biggest Business* (London: Eyre Methuen, 1975), p.301.

in 1970 and 98 per cent in 1950 (see Figure 4.4).[50]

As a result of these factors, the majors' profits also began to fall, so that in the 1960s they were forced to renegotiate their tax rate with their Middle East host governments, marking the transition from the first to the second era. Resenting the cut in oil tax revenues, the Middle East countries reacted by organizing politically in the form of the Organization of Petroleum Exporting Countries (OPEC) to demand a larger share of the lucrative oil industry.[51] OPEC's influence was at its peak during the 1973-74 oil embargo. The impact was greater than in previous crises because the United States was no longer the provider of last resort able to compensate for cutbacks by increasing its own production,[52] and without domination by the majors, coordination of supplies was more difficult.[53]

BP suffered greatly because its business had been heavily dependent on its crude oil production in the Middle East. With this taken away by nationalizations and renegotiations, BP's other operations could not compensate for these losses.[54] Shell,

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[50] Paul Stevens, 'A Survey of Structural Change in the International Oil Industry, 1945-1984', in David Hawdon, ed., *The Changing Structure of the World Oil Industry* (London: Croom Helm, 1985), pp.30-6; Levy, 'World Oil Marketing in Transition,' p.117; Jacoby, *Multinational Oil*, p.158; and Yergin, *The Prize*, p.515.

[51] Stevens, 'A Survey of Structural Change in the International Oil Industry, 1945-1984,' p.30; Tugendhat and Hamilton, *Oil, the Biggest Business*, pp.158-9; and Richard Bending and Richard Eden, *UK Energy: Structure, Prospects and Policies* (Cambridge, Cambridge University Press, 1984), p.14.

[52] Mary Ann Tetreault, *Revolution in the World Petroleum Market* (London: Quorum Books, 1985), p.34; Bending and Eden, *UK Energy*, p.13; Stourharas, *Are Oil Price Movements Perverse!*, p.50; Tugendhat and Hamilton, *Oil, the Biggest Business*, pp.206-9 and pp.291-2; Turner, *Oil Companies in the International System* (1984), p.206; Yergin, *The Prize*, p.436, pp.504-8 and pp.584-5; and Jeffrey Robinson, *Yamani: The Inside Story* (London: Fontana Paperbacks, 1988), pp.102-11; Maull, 'Oil and Influence,' pp.266-8.

[53] Levy, 'World Oil Marketing in Transition,' p.129.

[54] Shell Briefing Service, 'The Oil Majors in 1980,' No.5, 1981, p.8.

on the other hand, had a greater downstream operation, and was not as badly affected by OPEC's assertion of control over oil production in the Middle East. As Group Treasurer Howard McDonald explained: 'We always could sell oil better than we could find it, so in a sense the OPEC changes were a good watershed for us.'[55] Nonetheless, all companies were forced to become more international and more diversified. Responding to the increasing market forces, the majors responded by diversifying, fearing that without their oil cartel they would shrink. Not only did they expand their oil operations downstream, acquiring marketing networks in Europe and elsewhere, they also enlarged their tanker fleets, built refineries in Europe, and expanded into the field of petrochemicals.[56]

The rise of OPEC set in motion the forces leading to the third era - that of the free market. In the wake of the 1973-74 oil crisis and increasing oil prices, alternative sources of oil to those in the Middle East became not only desirable, but for the first time economically feasible as they existed in more difficult places for exploration and production. New sources were developed throughout the world, but the two largest finds were in Alaska and the North Sea. Thus, OPEC paved the way for its own demise, the price increases caused initially by the 1973-74 crisis led to significant changes in the industry, the diversification of sources of oil and the ever increasing number of companies made it virtually impossible for oligopoly control. Though OPEC remained a dominant player, by 1980, for the first time, the oil industry

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[55] Robert M. Grant, *The Oil Companies in Transition 1970-1987* (Milan: Franco Angeli, 1991), p.104 and pp.67-8.

[56] BP, *Our Industry Petroleum*, p.388.

became market driven.[57] As a result of the majors' diversification away from oil and the growth in the number of players in the oil industry, there was no one who could control price or supply swings. At the same time, the international oil network as a free-market became even more responsive to increased demand in the form of higher prices, thus marking the transition to the third era. In a free market, for a price, oil can be supplied quickly anywhere in the world.

Consequences for the British Government's Oil Strategy

There were three major consequences for the British government's policy options resulting from the changing oil industry structure. The first implication was that Britain's oil security considerations changed from those of an importer to those of a producer. As a producer in an increasingly unstable oil market, the British government like many other governments created a national oil company. In fact, over 23 state-owned oil companies, over half the world's total state-owned oil companies, were created between 1970 and 1982, while the rest were created before 1970.[58] Thus, the British government's creation of BNOC in 1976 can be seen as a response to this changing international situation. In addition to BNOC, the government could use access to the North Sea as a means of leverage to gain greater cooperation from the private oil companies. Department of Energy civil servants argued that the power of the British government in awarding exploration licenses to operate in the North Sea was the reason that Britain suffered less than other European

[57] Stourharas, *Are Oil Price Movements Perverse!*, p.51.

[58] *Financial Times International Yearbook, Oil and Gas*, 1992 and 1993.

countries during the 1973-74 oil crisis.[59]

Britain's economic security considerations also changed as Britain gained an enormous competitive advantage over most of its economic competitors who did not have domestic oil production and had to pay for oil imports. For example, from 1980 to 1985, France, Germany and Japan decreased their total oil consumption and yet the cost of their oil imports increased; for France from £10.7 billion to £12.5 billion, for Germany from £12.5 billion to £16.5 billion, and for Japan from £23.5 billion to £32 billion. Britain, on the other hand, went from paying £160 million in 1980 for oil imports to earning £7.7 billion as a net exporter in 1985.[60]

The second implication of the changing oil structure was the reduction of the value of ownership of BP. While the nature of a free-market ensured that oil would be delivered for a price, it also precluded an international company from favouring one country over another for nationalistic reasons - the means to retaliate were too great. Therefore, the government's ability to demand cooperation from the private oil companies in general increased due to the North Sea, and was more effective than investment in BP as a means of ensuring security of supply. As a successful international company, BP had repeatedly shown that it would not function as a national oil company. As previously mentioned, BP refused Prime Minister Heath's request to favour Britain during the 1973 oil crisis. Reinforcing BP's independent

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[59] Interview with Department of Energy civil servant; and Robert Stobaugh, 'The Oil Companies in Crisis,' *Daedalus*, Fall 1975, pp.192-3 and p.199.

[60] The figures are only general guides because all countries imported more than they consumed (i.e. refined and reexported some). Prices listed here are as if purchased on the spot market; the cost in each country varies according to the term of the contract, and taxes within the country. International Energy Agency, *Energy Statistics of OECD Countries, 1989-90* (Paris: OECD, 1992); and International Energy Agency, *Energy Prices and Taxes*, (Paris: OECD, 1992).

nature, a few years later, newspaper reporters revealed that BP and Shell had subverted the government's sanctions against Rhodesia from their inception in December 1965, which culminated in the establishment of the Bingham Inquiry in April 1977.[61]

The third implication was the force that OPEC continued to exert. Although OPEC's domination of the oil market was broken by the end of the 1970s, the organization's members still controlled a third of world production in 1980 and the majority of the world's oil reserves.[62] OPEC's emergence as an international power had many implications, including drawing attention to the British government's own involvement in the oil industry. This was domestically embarrassing because, as an oil producer, the government benefited from oil revenues which rose with the price of oil, but as an industrial country, Britain's many consumers suffered from high oil prices.[63] Through BNOC, the government soon found it had the ability to influence prices, but as an oil consumer, Britain did not want to be seen as a price leader.[64]

OPEC was at odds with Britain, especially as the price of oil began to fall in the mid 1980s. Continued British production and reduced prices, at least in

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[61] In March 1977 Martin Bailey published a report, 'Shell and BP in South Africa', see M. Bailey, *Oilgate* (London: Coronet Books-Hodder and Stoughton, 1979), pp.248-52.

[62] Levy, 'World Oil Marketing in Transition,' p.117; 'Foul Weather, Fair Friends,' *Economist*, 12 June 1982; and 'OPEC: I'll Huff and I'll Puff...Saudi Plans to Cut Oil Prices: OPEC Decides Upon New Production Ceiling,' *Economist*, 25 December 1982; 'After the OPEC Decade: Seven Sisters Who Lost Family Control: Future of the Oil Industry,' *Economist*, 15 October 1983; Lucy Kellaway, 'The First 100 Years: A Long Learning Process, the Oil Price Shocks,' *Financial Times*, 15 February 1988, p.60; and Turner, *Oil Companies in the International System*, 1984.

[63] Interview with Department of Energy civil servants and BNOC executives; and Jonathan Davis, 'The Arithmetic of North Sea Oil - Who Wins and Who Loses?' *Times*, 3 March 1992.

[64] Interview with Department of Energy civil servants.

appearance, undermined OPEC's effort to cut supply and raise prices, and drew hostile OPEC attention to the government's contradictory aims, regarding oil price and control and the free market. One BNOC executive recalled the political embarrassment caused when BNOC began to reduce its prices:

> The Saudis and the Nigerians were anxious and the government tried to stay out, but the Chancellor and Secretary of State had a few conversations with their counterparts.[65]

According to Nigel Lawson, Secretary of State for Energy from 1981 to 1983, OPEC officials were in constant contact with the government and applied pressure to get Britain to cooperate with them. In one extraordinary meeting, Ahmed Zaki Yamani, the Saudi Arabian oil minister, asked Lawson if Britain would like to join OPEC; Lawson declined. Yamani then got to the primary purpose of his visit and asked Lawson to cut Britain's oil production in order to keep OPEC oil prices from slipping further. Lawson explained that the government had no influence over the rate of production or prices, and claimed that it left the free market to decide.[66] In reality BNOC was actively setting the price for contracts on half of North Sea oil production at the time.[67]

The tension between OPEC and Britain continued. OPEC questioned the British government's denials of involvement in oil pricing, and threatened a price

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[65] Interview with BNOC executive; 'Where BNOC Leads: Cut in North Sea Oil Price,' *Economist*, 19 February 1983; 'Why Keep BNOC? Arguments for the Abolition of the British National Oil Corporation,' *Economist*, 2 April 1983; 'Sheikh Canutes: OPEC and Cuts in Oil Prices,' *Economist*, 6 October 1984; and 'OPEC Warns of Cuts in Oil Prices,' *Economist*, 17 October 1984.

[66] Lawson, *The View from No.11*, p.193.

[67] 'Why Keep BNOC? Arguments for the Abolition of the British National Oil Corporation,' *Economist*, 2 April 1983; and interviews with Department of Energy civil servants.

war. Because Middle East oil was (and still is) much cheaper to produce than off-shore North Sea oil, OPEC producers could make profits at much lower prices than North Sea producers. Britain therefore could not win a price war.[68] The British government's difficult position was only finally resolved with the sale of Britoil and the abolition of BNOC. OPEC's pressure, however, was not a primary cause of the government's sales; it was one of several contributory factors.

4.3. The Influence of International Organizations

Neo-liberal institutionalism and neo-functionalism contend that international institutions and supranational organizations play a significant role in affecting the international environment in which policy makers choose options.[69] Since the European Community (EC) and the International Energy Agency (IEA) are particularly large international organizations and have specific energy interests, we would expect them to be influential in this case. Surprisingly, I find that while economic interdependence between countries proved to be an influential factor, the EC and the IEA regulations were not.

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[68] 'Britain Shows OPEC the Way: Effect on OPEC of North Sea Price Cut,' *Economist*, 6 March 1982; 'Where BNOC Leads: Cut in North Sea Oil Price,' *Economist*, 19 February 1983; 'Being Nice to Nigeria: Production Quota Raised,' *Economist*, 14 July 1984; 'OPEC's Fellow Travellers Fall by the Wayside,' *Economist*, 19 January 1985; and 'OPEC Takes Rash Aim at Britain and Other Non-members: Cartel Threatens Oil-Price War,' *Economist*, 14 December 1985.

[69] Robert Keohane, 'Neoliberal Institutionalism: A Perspective on World Politics,' in Robert Keohane, *International Institutions and State Power* (Boulder, CO: Westview Press, 1989), p.3; Linda Cornett and James Caporaso, 'Interests and Forces in the European Community,' in James Rosenau, ed., *Governance without Government: Order and Change in World Politics* (Cambridge: Cambridge University Press, 1992), p.238; Ernst Haas, *Beyond the Nation-State: Functionalism and International Organization* (Stanford, CA: Stanford University Press, 1964); and R.J. Harrison, 'Neo-functionalism,' in A.J.R. Groom and Paul Taylor, eds., *Framework for International Co-operation* (London: Pinter Publishers, 1990).

Uncoordinated EC Energy Policy

The EC was founded on three distinct entities:[70]

- The European Coal and Steel Community (ECSC) set up by the Treaty of Paris in 1951;

- The European Economic Community (EEC) created by the Treaty of Rome in 1957; and

- The European Atomic Energy Community (Euratom) initiated by a second Treaty of Rome in 1957.

The concern for energy within the EC has been evident from the beginning; both the ECSC and Euratom dealt directly with energy. The ECSC focused on making the price of coal more competitive,[71] while Euratom focused on the development of nuclear power.[72]

Oil policy cooperation consisted of only a few directives, and little action was actually taken. The first specific measure was a proposal by the EEC Commission to create a common stockpile of petroleum in 1964. The original proposal (Directive 68/414/EEC) adopted in 1968 was to cover a 65 day period, which was extended to 90 days in 1972 (Directive 72/425/EEC). But the directive only took effect in January

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[70] They were founded by Belgium, Germany, France, Italy, Luxembourg and the Netherlands. Members who joined later were: Denmark, Ireland and Britain in 1973; Greece in 1981; and Portugal and Spain in 1986. The EEC, the ECSC and Euratom merged on 8 April 1964 to become the European Community (EC). C.D.E. Collins, 'History and Institutions of the EC,' in Ali M. El-Agraa, ed., *Economies of the European Community* Second Edition (Oxford: Philip Allan Publishers Limited, 1985), p.18.

[71] Romano Prodi and Alberto Clo, 'Europe,' *Daedalus*, Fall 1975, p.105; and Collins, 'History and Institutions of the EC,' p.14.

[72] Ali M. El-Agraa and Y.S. Hu, 'Energy Policy,' in Ali M. El-Agraa, ed., *Economies of the European Community*, Second Edition (Oxford: Philip Allan, 1985), p.253.

1975, too late for the oil crisis of 1973-74.[73] Britain did not join the EC until 1973, and was therefore only peripherally affected by these early developments.

EC Cooperation during the 1973-4 oil crisis was minimal. The major problems were the large discrepancies between members in terms of domestic resources and vulnerabilities. Germany and the Netherlands advocated coordinated responses, while Britain and France did not want to intervene. The EC countries were therefore left to scramble for oil supplies in competition with each other.[74] At the Energy Committee meeting prior to the November 1975 Energy Council, Henri Simonet, the Commissioner responsible for energy, castigated the nine members of the EC for their half-hearted efforts to adjust their national postures to facilitate a Community energy policy.[75]

Though the member states recognized that existing policies were insufficient, cooperation did not improve.[76] Over the period 1973 to 1985, the move towards a common EC energy strategy was hampered by the differences among member states in resources and energy priorities and by the reluctance of some member states to delegate part of their sovereignty to the Community.[77] These differences prevented

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[73] Robert Black, 'Plus ca Change, Plus C'est la Meme Chose: Nine Governments in Search of a Common Energy Policy,' in Helen Wallace, William Wallace and Carole Webb, eds., *Policy Making in the European Communities* (London: John Wiley, 1977), pp.181-83.

[74] Rodney Smith, 'International Energy Cooperation: The Mismatch Between IEA Policy Actions and Policy Goals,' in George Horwich and David Leo Weimer, eds., *Responding to International Oil Crises* (Washington, DC: American Enterprise Institute, 1988), p.20.

[75] Black, 'Plus ca Change, Plus C'est la Meme Chose,' pp.183-4.

[76] Report by the Commission in June 1983 as discussed in El-Agraa and Hu, 'Energy Policy,' p.258.

[77] B. Bourgeois, 'Energy,' in Willem Molle and Riccardo Cappellini, eds., *Regional Impact of Communities Policies in Europe* (Aldershot, Hants: Avebury, 1988), p.71; Ulf Lantzke, 'The OECD and Its International Energy Agency,' *Daedalus*, Fall 1975, p.217;

the EC from agreeing on internal energy questions or even presenting a united front in the International Energy Agency negotiations.[78] Britain was particularly obstructive of any coordinated action which meant sharing its oil, to the great frustration of other member states. The British government refused to sell North Sea oil to EC member countries at concessionary rates in normal times, and even refused to show a willingness to agree to policies concerning the size and stocking of reserves, or measures to ensure supplies to other EC countries.[79] Summing up the feelings of many of the member countries, a German official stated in 1979: 'Sooner or later Britain has to decide whether it is on the side of the Nine or OPEC.'[80] Ironically, the demands by the Europeans made the British government realize the need to control the North Sea. BNOC also provided a focal point for the EC and provided evidence that Britain could direct supply and prices despite the government's claims that they did not have the power to effect oil prices.[81]

More progress was made on energy policy in the 1980s by combining energy issues with other objectives such as foreign policy, environment, technological

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Robert O. Keohane, 'State Power and Industry Influence: American Foreign Oil Policy in the 1940s,' *International Organization*, Vol.36, No.1, Winter 1982, p.221, pp.225-6 and p.233; and G.John Ikenberry, *Reasons of State: Oil Politics and Capacities of American Government* (Ithaca, NY: Cornell University Press, 1988), p.81, p.88, and pp.90-94; 'National Security and Energy Link,' *Petroleum Economist*, May 1982, p.196; and interview with Department of Energy civil servant.

[78] El-Agraa and Hu, 'Energy Policy,' pp.255-6; and Prodi and Clo, 'Europe,' pp.107-8.

[79] David Deese and Linda Miller, 'Western Europe,' in David Deese and Joseph Nye, eds., *Energy and Security* (Cambridge, MA: Ballinger Publishing Co, 1981), p.200; El-Agraa and Hu, 'Energy Policy,' p.255; Prior and Clo, 'Europe,' p.107; and Richard Bailey, 'Unequal Shares in the North Sea,' p.331.

[80] Peter Norman, 'Britain Resisting EEC Pressure for Pledge on Higher Oil Production,' *Times*, 5 December 1979, p.19,

[81] Interviews with BNOC executive and Department of Energy civil servant.

advancement and regional development. By 1983, EC aid (subsidies and loans) represented 7.9 per cent of the gross investment in energy in Europe. The aid was distributed according to priorities determined by the EC's regional policy - not energy policy. This trend continued in October 1986 with the creation of the VALOREN program, whose goals included making regions less sensitive to disturbances in the traditional energy markets, such as oil. Because Britain had more opportunities for large-scale projects and was better able to present them to the Commission than countries less well-off, in energy terms, Britain received an exceptionally large amount of funds. This was particularly unusual given Britain's low priority status for regional assistance.[82] At the same time, Britain did not have to share the security and economic benefits of oil ownership. Had EC policy been better coordinated, funds for energy development might have been tied to greater security cooperation. Even these measures would not have been sufficient to effect the government's oil ownership decisions, either to halt the creation of BNOC or spur its demise. In addition, once created, there were too many other state owned companies within the member states for EC policy to apply pressure for its sale.[83]

Although the institutions designed specifically to address energy policy were ineffective, EC countries gained important advantages through other broader measures. First, the general EC non-discrimination legislation meant that companies registered in EC member states could bypass the DEn's requirement that all oil must

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[82] Bourgeois, 'Energy,' p.66-8 and p.85, footnote 1.

[83] Ikenberry, *Reasons of States*, p.81, p.88 and pp.90-93; also see, 'National Security and Energy Link,' *Petroleum Economist*, May 1982, p.196; Yergin, *The Prize*, quotes the headline of the *Middle East Economic Survey* in January 1974: 'Bilateral Deals: Everybody's Doing It,' p.629; and interview with Department of Energy civil servant.

be landed in Britain before being exported; and had to be treated without discrimination on licenses awards.[84] Second, EC commitments meant that communication between foreign and economic ministers was frequent which proved to be very constructive during crises by minimizing uncertainty and aiding cooperation.[85] While not directly affecting UK decisions to sell its oil assets, these factors may have helped to improve the oil market that in turn reduced the number and severity of oil crises.

European Community Economic Interdependence

Although Britain did not enter the EC until 1973, it steadily became more dependent on EC member states from the 1960s on so that by the 1980s approximately 60 per cent of legislation made in Britain at the national level involved European Community issues.[86] The trend is also quantifiable in the trade statistics; Table 4.1. shows that both exports and imports have become more heavily concentrated on Britain's EC partners.[87] In addition, Britain's trade with the U.S. and Japan has declined markedly so that by 1988 only 11 per cent of British imports

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[84] The landing requirement was more theoretical because any request for a waver were approved. Interviews with Department of Energy civil servants and minister.

[85] Prodi and Clo, 'Europe,' pp.106-7.

[86] Paul Taylor, *International Organization in the Modern World: The Regional and the Global* (London: Pinter Publishers, 1993), p.93.

[87] William Wallace, *Britain's Bilateral Links within Western Europe* (London: Routledge and Kegan Paul, 1984), p.1; and Ian Budge, David McKay, Rod Rhodes, David Robertson, David Sanders, Martin Slater, Graham Wilson, *The Changing British Political System: Into the 1990s*, Second Edition (London: Longman, 1988), pp.140-157 and p.227; Alan Winters, 'Britain in Europe: a Survey of Quantitative Trade Studies,' in Alexis Jacquemin and Andre Sapir, eds., *The European Internal Market: Trade and Competition* (Oxford: Oxford University Press, 1989), p.122.

Table 4.1.
British Exports to and Imports from EC Member Countries
Percent of Total UK Trade

	1957	1974	1981	1986	1988
Exports to EC	14.6%	33.4%	41.2%	47.9%	62%
Imports from EC	12.1%	30.0%	39.4%	50.4%	64%

Source: Ali M. El-Agraa, 'Basic Statistics of the EC,' in Ali M. El-Agraa ed., *The Economics of the European Community*, Third Edition, (Oxford: Philip Allan Publishers Limited) 1990, p.61-2.

came from the United States and 6.1 per cent from Japan, while 12.9 per cent of British exports went to the United States and 2.2 per cent to Japan.[88]

The evidence from this case supports Paul Taylor's contention that the British government formulated its energy policies with consideration for its EC partners, but not because of specific legislation.[89] In other words, the forces of economic interdependence that provided the impetus for the EC have also led to the adoption of common policies across Europe. This explains why, as Alan Walters (Mrs. Thatcher's economic advisor from 1981 to 1983) has pointed out, all European countries reduced their adjusted borrowing and experienced fiscal contractions in recessionary conditions on a scale similar to Britain's.[90] In addition, across Europe (France and Germany) and the industrialized world (Canada to New Zealand), there

[88] T. Hitiris, 'Trade Policies,' *European Community Economics*, Second Edition (London: Harvester Wheatsheaf, 1988), p.208; also see Winters, 'Britain in Europe,' pp.125-6.

[89] Taylor, *International Organization in the Modern World*, p.94 and p.106.

[90] Alan Walters claims that Britain's economic tightening was less severe than others, but this only holds true with some calculation adjustments. Alan Walters, *Britain's Economic Renaissance: Margaret Thatcher's Reforms 1979-1984* (Oxford: Oxford University Press, 1986), pp.96-7.

was interest in asset sales. Very few countries sold assets in the early 1980s most waited until the late 1980s or did not sell at all.[91]

There is no evidence that EC laws restricted the British government's decision to sell its oil assets, yet the broader interdependent ties may have influenced the thinking of some civil servants and politicians in Britain. For example, during the 1973-74 oil crisis, Prime Minister Heath did not pass a law to require BP to favour Britain with oil supplies for, among other reasons, fear of antagonizing Britain's EC partners. Similarly, a DEn civil servant explained that Britain's official position on oil prices was for lower prices because Britain could not overtly side with OPEC when higher prices would hurt its new European partners.[92]

EC company legislation, however, has had a peripheral effect on BNOC's evolution. The first time EC regulations were a factor was in 1976 when BNOC and the participation agreements were being created. There were concerns that BNOC's objective of supplying Britain in a crisis was inconsistent with international obligations, specifically free trade in the EC.[93] Although the issue was raised by the Conservatives who opposed the creation of BNOC, it was not a major point of contention nor sufficient to delay the creation of the national oil company. BNOC was not in absolute control because there were other companies operating in the North Sea, there was oil from the Middle East and elsewhere, and the arrangements were only voluntary commercial agreements. Technically, BNOC could not be challenged,

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[91] Survey of privatization as reported in *Economist* and the *Financial Times* using Profile, 1983-1992.

[92] Interview with Department of Energy civil servant.

[93] Lord Strabolgi, *Hansard Parliamentary Debates (Lords)*, 9 November 1976, vol.377, col.182-185 and 18 November 1975, vol.377, col.1459-1460.

but as one DEn official observed, the government was always afraid it would be.[94]

The EC's classification of public companies and take-over laws also affected the form taken by British privatization. The government avoided retaining more than 50 per cent in companies in part because they would be classified as public companies in the EC, making the British government liable for debts of the enterprise.[95] EC takeover laws affected the government's decisions with what they omitted. While member states could not forbid a takeover offer launched by an EC investor, there was no such rule prohibiting intervention in bids by non-EC corporate bodies.[96] This was a useful outlet in 1987 when ministers referred the case of Kuwait Investment Office's purchase of 21% of BP shares to the Monopolies and Mergers Commission (MMC). Since KIO was not a member of the EC, it was not discriminatory for the MMC to rule against KIO and force it to reduce its shareholding in BP to below 10 per cent.[97] The effect of company legislation was limited, however, because there was little that was more restrictive than pre-existing British law. In fact, much of EC company law was based on British practice. EC legislation on takeovers, for example, was similar to Britain's City Code on Takeovers and Mergers.[98]

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[94] *Hansard Parliamentary Debates (Lords)*, 9 November 1976, vol.377, col.183; and 18 November 1976, vol.377, col.1459; and interview with BNOC executive.

[95] Gardner, *Decade of Discontent*, p.20.

[96] Confederation of British Industry, *Company Law and Competition* (London: Mercury Books, 1989), p.43.

[97] Steven Butler, 'Divorce With a Degree of Dignity: The Way BP has Cleared Up the Problems Created by the KIO's Shareholding,' *Financial Times*, 4 January 1989, p.17; and 'Survey of Arab Banking: Working in the Spotlight - The Kuwait Investment Office,' *Financial Times*, 24 October 1988, p.41.

[98] CBI, *Company Law and Competition*, p.42.

The International Energy Agency

In the wake of the 1973-74 oil crisis, Britain as an oil consumer was active in the creation of a new type of organization, distinct from EC initiative? The IEA was formed by 16 industrialized countries including the United States, Japan, and most EC countries, but not France who disagreed with the organization's approach.[99] In addition to keeping records and providing a means for communication between countries, the main feature of the IEA was the oil sharing mechanism, called the Emergency Management System (EMS). Through the EMS all members were committed to reduce oil demand and to share available oil in the event of any significant disruption in the world oil supply, defined as a 7 per cent loss of normal supply by one or more member countries. The IEA also required every member country to maintain reserves enabling it to sustain consumption for 90 days without oil imports.[100] Britain had the advantage of the North Sea, which had enormous reserves. Stockpiles maintained on-shore were costly, and most countries passed this responsibility and cost on to the oil companies. As a result the stocks were usually industry working stocks, such as oil waiting to be refined, and therefore not truly

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[99] The original signers of the IEA agreement in November 1974 were: Austria, Belgium, Canada, Denmark, Ireland, Italy, Japan, Luxembourg, The Netherlands, Spain, Sweden, Switzerland, Turkey, United Kingdom, United States and West Germany. Greece, New Zealand and Norway joined in 1976-77, Australia in 1979, and Portugal joined in 1980. The only OECD countries who are not members of the IEA are France, Finland and Iceland. Smith, 'International Energy Cooperation,' p.21; and Deese and Miller, 'Western Europe,' p.200.

[100] Peter Ellis Jones, *Oil: A Practical Guide to the Economics of World Petroleum* (Cambridge: Woodhead-Faulkner Ltd, 1988), pp.232-38; International Energy Agency, *The International Energy Agency* (Paris: IEA/OECD, 1983), p.16; Smith, 'International Energy Cooperation,' pp.28-31.

surplus.[101]

After North Sea oil came on line (1975) Britain was pressured to share its oil resources with fellow members, which made the British government more possessive. The government feared that their present comparative strength in oil supplies would commit them in advance to put substantial North Sea oil supplies at the disposal of other IEA countries.[102] This pressure by the IEA is illustrated by the way it calculated its statistics. The international organization treated any energy resource within western Europe as indigenous to every country in the region. Thus, oil and gas produced by Britain and Norway were assumed to remain in western Europe and to be immediately available to all western European consumers, without entering into international trade, which was far from the actual case.[103]

BP and Shell were also very active participants in the development of the IEA mechanism. For the oil companies, an equitable distribution of oil, such as during the 1973-74 crisis, was in their best interests.[104] The decline of the majors' control over oil supplies meant that they were no longer able to enforce such a system on their own. The IEA formal mechanism enabled the large number of companies entering the international industry to coordinate oil distribution where they might not have been

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[101] Edward Krapels and Sarah Emerson, *Storage in the International Oil Market*, Special Report No.1117 (London: The Economist Intelligence Unit, 1987), pp.31-2; and David Blair, 'The International Energy Agency: Problems and Prospects,' in Gasteyger, ed., *The Future for European Energy Security*, p.117; and 'Stocks for Crisis Management,' *Petroleum Economist*, October 1982, p.398.

[102] Interview with Department of Energy civil servant; Deese and Miller, 'Western Europe,' p.199; and El-Agraa and Hu, 'Energy,' p.255.

[103] Ian Smart, 'European Energy Security in Focus,' in Gasteyger, ed., *The Future for European Energy Security*, p.150.

[104] Interviews with Department of Energy civil servant and BP executive.

able to otherwise. According to the IEA over 200 national and international companies and 21 countries participated in the 1978 Second Oil Allocation Systems Test.[105] Real cooperation, however, was limited by U.S. anti-trust legislation which prevented American companies from divulging information on oil pricing.[106] Given this fact, one British civil servant explained that the IEA had nothing better to do than prepare and practice, but that the efforts were only 'paper exercises'.[107] The IEA's oil sharing mechanism has never been tested. Even during the 1979 oil crisis and Sweden's 17 per cent shortfall the formal sharing arrangements were never enacted.[108] Because some members (such as Britain) would have refused to cooperate if the formal mechanisms had been enacted, the Agency instead resorted to attempts at informal coordination, consultation and advice,.[109]

The 1979 crisis was alleviated and the drastic price rises avoided due to the willingness of Saudi Arabia to increase production, the high level of oil stocks and weakness in demand, and through IEA information-sharing and strong (but general) statements.[110] Within the DEn the IEA received no credit for smoothing the chaotic international oil turbulence, and a few civil servants even made jokes about the

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[105] Blair, 'The International Energy Agency,' p.116; and IEA, *International Energy Agency*, p.25.

[106] Blair, 'The International Energy Agency,' p.117.

[107] Interview with Treasury civil servant.

[108] Although seasonal adjustment brought Sweden's shortfall to 9.8%, it was still above the 7% threshold. Blair, 'The International Energy Agency,' pp.112-3; Smith, 'International Energy Cooperation,' pp.35-38; and Keohane, *After Hegemony*, p.229.

[109] Keohane, *After Hegemony*, pp.231-36; and Smith, 'International Energy Cooperation,' pp.68-84.

[110] Keohane, *After Hegemony*, pp.236-7. Information sharing and top level coordination were confirmed by Department of Energy civil servant.

organization. Only one civil servant suggested that the IEA mechanisms actually alleviated the need for BNOC, though several DEn civil servants recognized that some of their powers were being delegated to the IEA, such as the collection of statistics which occurred in the mid 1980s.[111]

Britain's resistance to oil sharing measures can be understood when the specific costs of sharing are recognized. Rodney Smith has calculated that per capita net losses from oil sharing for Britain in the early 1980s would have been $4.02 with a 7 per cent supply disruption and $5.56 with a 15 per cent supply disruption, while net gains would have accrued to Belgium, Denmark, Germany, Luxembourg, Sweden and Switzerland. Only Japan and the United States would have remained relatively unaffected.[112] Despite minimal action by the IEA, the fact that it exists and that Britain is an active member illustrates that the member countries involved acknowledge their interdependence and the broader costs of not cooperating. As one DEn civil servant explained, Britain could see that even as an oil producer, not agreeing to share would hurt the world economy which would then hurt Britain.[113]

Conclusion

Although systems level models can explain why Britain was more susceptible to international pressures on financial issues and less so on oil issues from 1975 to 1985, these types of models can not explain the specifics, such as the 1976 IMF

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[111] Interviews with Department of Energy civil servants; and Lawson, *A Radical View from No.11*, p.163.

[112] Smith, 'International Energy Cooperation,' pp.52-3.

[113] Interview with Department of Energy civil servant; Smith, ('International Energy Cooperation,') however, argues that this is fortunate for energy security and oil consumers because IEA measures would have worsened the situation (pp.68-84).

crisis, or change, such as the shift from an oil oligopoly to an free market for oil. A systems level model does, however, highlight the fact that states work within constraints beyond their immediate control, and that a country's position in the international system sets the parameters for the policy options available to politicians. This proved to be true for Britain in the case of its oil assets, where the international financial situation and the structure of the international oil industry narrowed the range of what was possible, though only its financial position in 1977 had a direct impact. Though membership in international organizations was not specifically an influence, economic interdependence was, through a self-interest in the welfare of its trading partners. By focusing on an issue, the role of international organizations is already included. Studying organizations separately is less revealing. As Susan Strange has argued: the study of regimes or international organizations is 'obfuscating and confusing instead of clarifying and illuminating, and distorting by concealing bias instead of revealing and removing it.'[114]

The effect of international factors on the British government's decision to sell its oil assets can be illustrated with a Venn diagram, in which the intersection of circles represents the overlap of international parameters which sets the range of policy options (see Figures 4.5 and 4.6). The three international level variables examined in this case are represented by circle 1 for the policy options possible with the international financial position of Britain, circle 2 for policy options possible with Britain's position in the international oil industry, and circle 3 for the policy options consistent with Britain's membership in international organizations. In both figures,

[114] Susan Strange, '*Cave! Hic Dragones*:A critique of Regimes Analysis,' in Stephen Krasner, ed., *International Regimes* (Ithaca, NY: Cornell University Press, 1985), p.337.

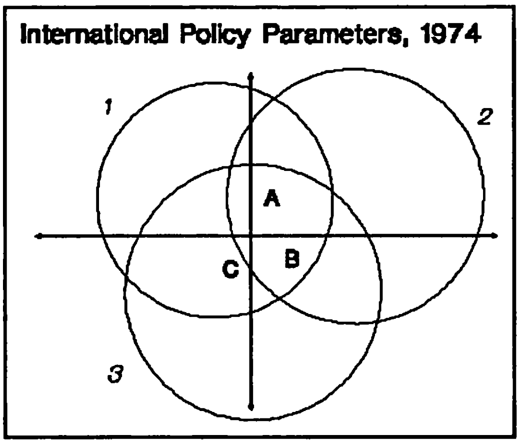


Figure 4.5.

point A represents the policy to increase taxes, point B represents the policy to increase the budget deficit and point C represents the policy to sell oil assets. In 1974, just after the 1973 oil crisis, selling oil assets was not possible (as illustrated in Figure 4.5 by the exclusion of point C from circle 2.) In 1977 the oil situation had changed so that a sale was possible as ownership was less effective in the free market (point C now included in circle 2 of Figure 4.6). As a result of severe balance of payments deficits and IMF intervention, however, Britain's international financial position had changed so that a budget increase was no longer possible (point B excluded from circle 1 in Figure 4.6).

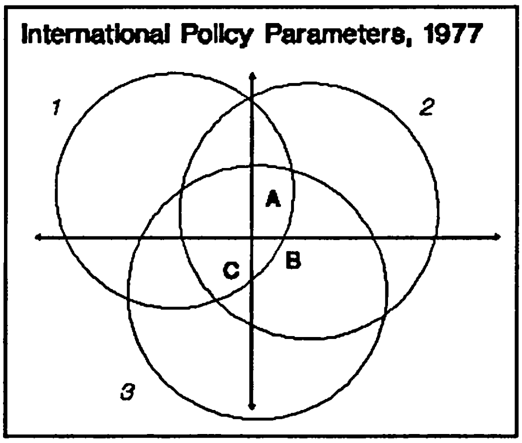
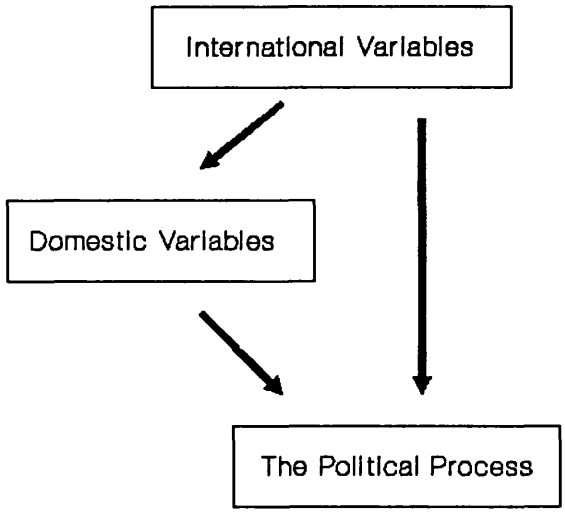


Figure 4.6.

Though the international level played an important role, it alone did not determine the government's options, contrary to international systems scholars claims. It is, therefore, necessary to look at other sets of intervening variables, which however were also influenced by international factors. The full force of international pressure includes both the direct and indirect effects, as illustrated in Figure 4.7. In the next chapters I examine sets of intervening variables and how these sets of parameters affected Britain's politician's decision to sell the state's oil assets. The three sets of variables are the management of the oil companies in Chapter Five, and the civil servants in Chapter Six, and the political process in Chapter Seven.

Figure 4.7: The Direct and Indirect Effect of International Variables



Chapter Five: Structure, Motivations and the Managers of the State-Owned Oil Companies

Applying the conventional public choice models of individuals as economic utility maximizers to the managers of Britain's state-owned oil companies, we would expect them to welcome privatization, as a move to the private sector would allow greater financial freedom for their company and higher salaries for them personally. Yet many managers actually impede privatization. Their resistance is often listed in the privatization literature as an obstacle to privatization but without an explanation as to why, or more specifically why some managers are not opposed and why some are more successful in achieving their preferences.[1] One of the reasons the role of the managers has not been satisfactorily analyzed is that they do not fall into standard categories of analysis. Though the managers of state-owned companies are not private sector employees but rather state employees subject to ministerial directives, and partly supported by central government funds, they are not normally included in analyses of government bureaucracies.[2]

Initial differences between the managers' reactions can be understood from the differences between types of companies. As Yair Aharoni has pointed out, not all state-owned industries are alike.[3] In the British case there were three distinct types of companies: the Morrisonian public corporation, the semi-detached corporation and

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[1] Vickers and Yarrow, 'The Politics of Industrial Privatization in Western Europe,' pp.18-9.

[2] Interviews with BNOC and BP executives; Aharoni, *The Evolution and Management of State Owned Enterprises*, p.5; and Gavin Drewry and Tony Butcher, *The Civil Service Today*, Second Edition (Oxford: Basil Blackwell, 1988), pp.16-7.

[3] Aharoni, *The Evolution and Management of State Owned Enterprises*, p.396.

the virtually private company. BGC was a traditional Morrisonian corporation created to serve the public interest while being run along commercial lines, breaking even one year with another. The company's charter was (re)created by Acts of Parliament in 1948, 1965 and 1972 which ensured government control over national assets, and its directors, appointed by ministers, were to 'regard themselves as the high custodians of the public interest.'[4] BNOC was created much later than the traditional Morrisonian corporations and with closer attention to fiscal control and economic efficiency. As such, though still created by an Act of Parliament, BNOC's domain was more narrowly defined and more tightly controlled, both by legislation and by operating in the private-sector oil industry.[5] BP represents the third type, a virtually private-sector company. As a Companies-Act company, the government acted only as a large shareholder and was not involved in the day-to-day running of the business.[6]

These fundamental structural differences help explain why different strategies are rational for different managers and suggest why some mangers are more likely to be successful than others. Aharoni identifies the major variables that explain the

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[4] H. Morrision, *Socialisation of Transport*, (1933) as quoted in Cento Veljanovski, *Selling the State, Privatization in Britain* (London: Weidenfeld and Nicolson, 1987), p.58; David Heald, 'The United Kingdom: Privatisation and its Political Context,' in John Vickers and Vincent Wright, eds., *The Politics of Privatisation in Western Europe* (London: Frank Cass, 1989), p.34; Lynn Pearson, *Organization of the Energy Industry* (London: Macmillan, 1981), p.98; and interviews with British Gas Corporation executives.

[5] Department of Energy, 'About Britoil,' 1978; BNOC, *Annual Report*, 1976; and Aharoni, *The Evolution and Management of State Owned Enterprises*, pp.13-5.

[6] Heald, 'The United Kingdom: Privatisation and its Political Context,'p.34; Bradbury and Bridges letters; and Aharoni, *The Evolution and Management of State Owned Enterprises*, pp.13-5.

differences within the state-owned industries group.[7] Extrapolating from these variables, I argue that there are three factors that influence how managers react to the possibility of privatization, and how effective their support or opposition is. These factors are organizational autonomy, financial independence, and success in achieving its missions - either profit or national interest.[8] The consequences of these factors are summarized in Table 5.1.

In terms of organizational autonomy, all companies desire to be autonomous and will resent any governmental interference in the organization. Managers will therefore employ tactics to maintain the company's autonomy, while managers of less autonomous companies will seek to become more self-sufficient through means including: making commercial agreements with the private sector, expanding internationally and retaining profits by spending or reinvesting them, as well as urging the government to sell the company to the private sector. Managers will react positively to privatization as it represents another means to increase their autonomy. A company's chances of privatization increase the more self-sufficient the company, as less autonomous companies are harder to transfer to the private sector.

Managers of companies which are financially independent seek to remain that way and employ the same tactics as autonomous companies. Managers of companies which depend on government finance may, however, resist a move to the private

[7] Aharoni, *The Evolution and Management of State Owned Enterprises*, pp.396-400.

[8] National interest: 'The concept of the security and well-being of the state', Jack Plano and Milton Greenberg, *The American Political Dictionary*, Eighth Edition (New York: Holt, Rinehart and Winston, 1989), p.498.

A more cynical definition: 'The cause in which political leaders claim to be acting when pursuing a policy unpopular with the electorate or with other states - or especially when pursuing their own interests.' Nicholas Comfort, *Brewer's Politics: A Phase and Fable Dictionary* (London: Cassell, 1993), p.401.

Table 5.1. Company Status and Objectives

Company Status	Management's General Objectives	Management Tactics in Response to Privatization Proposals	Likelihood of Privatization
Organizational Autonomy			
- High	- Maintain autonomy	- distance itself from the government - make private sector agreements	High
- Low	- Increase autonomy	- expand internationally - retain profits	Depends on mission
Financial Independence			
- High	- Maintain independence	- same as high autonomy	High
- Low	- Obtain financial support	- seek government investment - seek private sector investment	Low
Success in Achieving Mission			
- Profit	- No government intervention	- same as high autonomy	High
- National Interest	- Retain government mandate for national interest mission	- achieve highest standards - publicize service provided - delay government efforts - lobby against privatization	Low

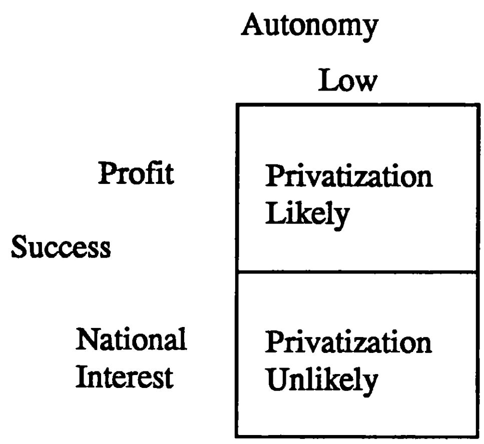
sector as it could mean selling off their assets, closing down the company and ultimately unemployment. They will most likely resist privatization using delaying tactics and lobby government ministers so as not to lose their financial backing.

The management of companies which successfully achieve their mission, either achieving high profits or providing a recognizable national service, fight to keep their company together as an entity. Success breeds loyalty and pride. The management of a company with a profit mission have limited allegiance to their government owners and thus may prefer private ownership, but they will definitely react strongly against any action that breaks apart the company or limits its future potential. In contrast, the managers of a company with a national interest mission depend on government ownership for a justification of their non-profit mission, and therefore seek ways to maintain that mandate including highlighting the usefulness of the service they are providing and continuing to improve the service. The result is less clear for managers of companies who have been less successful in achieving their missions. Depending on their financial independence and organizational autonomy, they may be frustrated and therefore may be more willing to consider alternatives, including privatization, or they may be fearful for their future, and thus resist change.

The ability of managers to influence policy outcomes is also affected by the company's structure. Managers in companies with high levels of financial or organizational independence have a greater ability to persuade the government to implement their preferences, while managers of a company that is financially dependent with little success in achieving its mission will be less able to influence the government (see column three in Table 5.1.)

Finally, these three factors affect the degree of difficulty a government will have in selling a company. The companies where the feasibility of a sale is highest are those which are financially and organizationally independent and operate with a profit mission because the management has no significant ties to the government and sees gains from the sale. (See the last column in Table 5.1.) The most difficult to sell are those with a national interest mission and either low organizational autonomy or low financial independence because they rely on the government to function and would suffer costs from a sale (see Figure 5.1).

Figure 5.1. Low Organizational Autonomy Versus Mission



5.1. British Petroleum Under Threat

By the 1970s, BP was financially independent from the government, successfully established internationally and struggling to redirect itself into more profitable areas. The company's independence was threatened in two ways; by an increase in the government's share ownership and by the need for new capital. These precipitating conditions led the management to reconsider the costs and benefits of government ownership.

Fear of Government Reasserting Control

The government's holding in BP decreased steadily over time (see Figure 5.2). In fact, from the 1950s, BP had a strategy of increasing the total capital of the company in order to dilute the government's shareholding. As BP expanded, it issued new shares to pay for purchases, such as the Trinidad Petroleum Company in 1955, Apex (Trinidad) Oilfields in 1960, Kern Oil Company in 1961, an asset purchase from the Distillers Company in 1967, and a merger with Super Test Petroleum Corporation in 1971.[9] As one BP executive recalled:

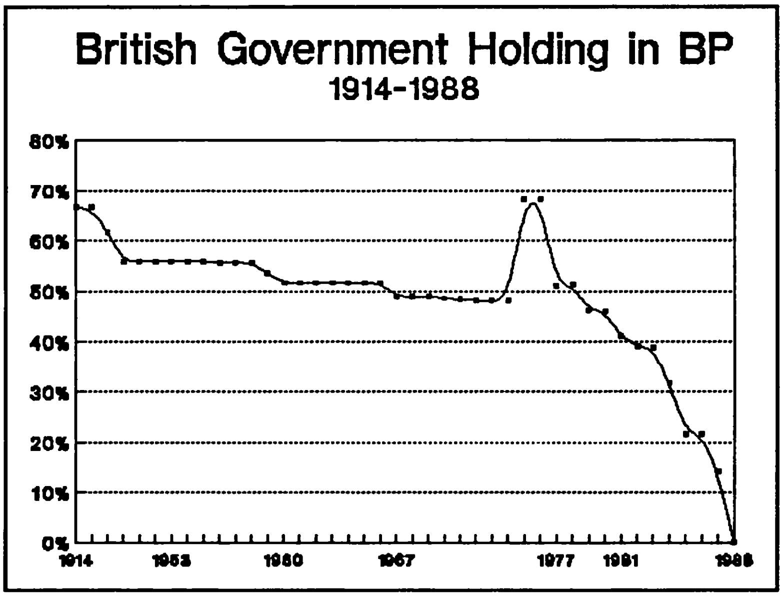


Figure 5.2.

> If you look at when Morris Bridgeman was chairman, he was always keen to hit the 49 per cent spot...There were various attempts, at various times, to use shares to purchase companies with the thought that the small change might bring HMG [Her Majesty's Government]'s holding below 51 per cent. It was all part of eroding the government's shareholding.[10]

It was in fact under Bridgeman in 1967 that the government's shareholding dropped

[9] BP, *Annual Report and Accounts*, 1955-1971.

[10] Interview with BP executive.

to 48.9 per cent due to the issue of new shares to purchase the chemical and plastics interests of the Distillers Company.[11] Government ministers assisted in these efforts by not subscribing to two of BP's new share issues, in 1957 and 1981.[12]

Why BP followed this strategy of reducing the government's stake is not clear. The views of senior BP executives were mixed. Some argued that the 50 per cent mark was not necessarily important because it had no legal significance. The company's Articles of Association, not the size of the government shareholding, gave the British government the veto and put two ministerial nominees on the board of directors.[13] Others pointed out that government ownership did make a difference to BP's operations abroad. Some countries such as Venezuela and Guatemala refused to allow foreign government owned oil companies to operate in their territory. This impact was evident by the fact that as soon as the British government sold 5 per cent of its BP shares in 1979 bringing the total down to 46 per cent, BP became eligible to operate in Venezuela and immediately set up facilities there.[14]

The best explanation of the management's attitude, however, is that there was an ideological or psychological barrier to government ownership over 50 per cent.[15] The management valued its independence, and government ownership over 50 per cent threatened their image of themselves as an sovereign company. The managers perceived that government ownership handicapped them, limiting their decisions

[11] BP, Chairman's Statement, *Annual Report and Accounts*, 1966, pp.6-7 and p.21.

[12] *Hansard Parliamentary Debates (Commons)*, 20 December 1957, vol.580, col.135.

[13] Interview with BP executive.

[14] Interview with BP executive.

[15] Interview with BP executive.

unnecessarily. These feeling came through as late as Sir Peter Walters speech to BP's shareholders after buying back KIO's holding in BP in 1989. The emphasis was on independence - from any government.[16]

When the government purchased Burmah Oil's holding in BP, thereby raising its holding to 68 per cent - more than two-thirds of the company's equity - BP's managers were shocked and dismayed to learn that their reduction policy had been drastically reversed in a single day. BP, in fact, had always disliked having Burmah as a major shareholder. One BP executive explained:

> [We] had to have a couple of Burmah chaps on the board who never contributed anything...I'd always been wondering how we could shake Burmah off our backs who had no particular oil expertise but had this say... [they] just got a dividend and passed it on to their own shareholders.[17]

When Burmah ran into financial difficulty in 1974, company executives approached BP managers to determine whether BP would be prepared to take over Burmah. BP could not have bought back its shares from Burmah, however, because there were laws against it at the time (these have since changed). Instead, BP was offered some of Burmah's properties.[18] But after examining Burmah's accounts, BP executives realized that the situation was far worse than had been conveyed, so disappointedly, they were forced to decline the offer. One BP executive counselled Burmah to go 'very quickly to the Governor of the Bank of England.'[19]

Burmah did go to the Bank of England, and as part of the rescue plan, the

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[16] 'Shareholders Support BP Buy Back,' *Financial Times*, 1 February 1989, p.25.

[17] Interview with BP executive.

[18] Interview with BP executive.

[19] Interview with BP executive.

Bank purchased Burmah's holding in BP. Though the BP managers knew of Burmah's troubles and even recommended that they go to the Bank, they did not suspect the result would be an increase in the government's holding in BP. As one BP executive complained:

> It's one thing to have your 51% but to have a majority as big as that for the government would have made it too much of a temptation for the government to break the Bradbury letter agreement. I wasn't very keen on that. Not that I was consulted as I remember.[20]

The chairman of BP, Eric Drake, was furious. He demanded on several occasions in writing and in person to the Prime Minister that the shares be sold.[21] One such documented occasion was on 15 July 1975 when Drake told Benn that the government's holding must be kept below 50 per cent, otherwise it would destroy BP's credibility in the US, New Zealand and elsewhere (BP operated in over 80 countries).[22]

Exacerbating BP's fear of increased government ownership was the fact that the share increase occurred under a Labour government, which included Tony Benn as the Secretary of State for Energy, who advocated socialist measures such as nationalization. Benn increased BP's fears of government intervention by questioning the structure of the relationship between BP and the Treasury and proposing policies such as participation that sounded all too similar to the measures that had abolished their oil concessions in the Middle East.[23] As one BP executive explained: 'Obviously we wanted the government around less, especially because Benn had made

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[20] Interview with BP executive.

[21] Interview with BP executive; BP, *Annual Report and Accounts*, 1975, p.6.

[22] Benn, *Against the Tide*, p.419.

[23] Interview with BP executive.

us aware of the threat the government's stake could present.'[24] The fear was reinforced by the impression that BP executives gleaned when visiting Benn's office. One BP executive described the horror of finding BP included on a wall chart of government owned energy industries, and commented: 'But Benn didn't own BP, the Treasury did.'[25] BP was thus on alert for the possibility that partial government ownership could evolve into a complete takeover, or nationalization, of the company.

All of the BP executives who I interviewed pointed to the Bradbury letter as the guiding principle of the relationship between BP and the government. To BP, this letter meant that the government would not intervene in the running of the company, and that autonomy was valued highly at BP.[26] Whenever the party in power changed, BP made a point of getting a question asked in Parliament about the government's policy towards BP. In 1975, a BP company memo stated: 'As we all know, what we want is ... an unequivocal statement in the House of Commons that the practice of non-intervention, non-interference is to continue.'[27]

In fact, the Bradbury letter and the subsequent Bridges letter (1951) are vague agreements that in reality failed to rule out direct intervention into BP's affairs. For example, the government agreed not to use its right of veto except if BP's activities of the company affected the government's foreign, naval or military policy; or the company's status changed; or BP planned new activities with control implications; or

[24] Interview with BP executive.

[25] Interview with BP executive; also see Bradbury letter in Appendix I which defines BP's government contacts as the Treasury and the Admiralty.

[26] Interview with BP executives.

[27] BP memo, December 1975. See also statements in *Hansard Parliamentary Debates (Commons)*, 29 April 1965, 26 February 1969 and 18 March 1974.

where fuel oil was sold to foreigners in a situation which might endanger the fulfilment of current Admiralty contracts. (See the copy of the Bradbury letter in Appendix I.) The letter does not elaborate on these exceptions; they are, therefore, open to interpretation.

Thus, it was not the Bradbury letter per se, but the Treasury's interpretation of that letter that has been the foundation of the non-intervention relationship between BP and the government. BP saw the Treasury as being a defender of their independence because they profited from the investment in BP and had developed a satisfactory working relationship over decades.[28] As one BP executive explained: 'The Treasury was the department responsible for our shareholding; and they couldn't have cared less what we did as long as we went on being a profitable and successful and efficient company.'[29] When Benn came into office, he questioned not only the Treasury's relationship with BP, but the interpretation of the Bradbury letter itself. A review of the House of Commons debates shows that while the government's ownership had been controversial over time, Benn was the first to question the structure of BP's relationship with the government.[30] Benn argued that the government should use its now dominant shareholding to control the company and the shareholding should be transferred from the Treasury to the Department of Energy as part of a move to make BP into a national oil company.[31]

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[28] Interview with BP executive.

[29] Interview with BP executive.

[30] Review of all discussion of BP as listed in the index to *Hansard Parliamentary Debates (Commons and Lords)*, 1913-1977.

[31] Interviews with Department of Energy and Treasury civil servants and Labour ministers; Blackstone and Plowden, *Inside the Think Tank*, p. 81; Geoffrey Fry, *The Changing Civil Service* (London: George Allen & Unwin, 1985), pp.15-7.

BP executives saw their independence being threatened by this challenge to the Bradbury letter, and thus lobbied hard against the Department of Energy controlling the BP shares and against becoming a national oil company.[32] In addition to the problems of increased government ownership, out right nationalization could mean retaliation against their downstream operations in Europe and production interests in Alaska.[33] Aiding BP's efforts was the fact that the company had the specific goal of getting the government to sell its shareholding, and several means to achieve it.[34] In addition to contacts with the top level civil servants, BP also had political connections. As one BP executive explained: '[We] had access to the Prime Minister, the Chancellor, the Foreign Secretary or any other minister...at the drop of a hat.'[35] Though not contributing directly to the Conservative party, as part of a complex relationship with the government, BP was a large public contributor remaining one of the top five contributors to charity in Britain, with contributions rising from £500,000 in 1979 to £14.5 million in 1992.[36] Though, as one of the ten largest companies in Britain, in terms of revenue and profit, BP is a company that no

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[32] Interview with BP executive.

[33] Turner, *Oil Companies in the International System (1978)*, p.120; and Turner, 'State and Commercial Interests in North Sea Oil and Gas,' p.97.

[34] Wyn Grant, 'Business Interests and the British Conservative Party,' *Government and Opposition*, Vol.15, Spring 1980, p.157.

[35] Interview with BP executive.

[36] In 1979 BP was the fifth largest public contributor, in 1986 and 1987 BP was the largest, and in 1992 BP was second only to BT. 'Big Increases in Firms' Charity Handouts,' *Independent*, 3 February 1993; 'Big Companies Reduce their Gifts to Charity,' *Independent*, 17 January 1989; 'Charitable Britain,' *Economist*, 26 December 1981. Some charitable gifts can be linked to political causes. For example, from 1984 to 1987 BP contributed to the Industrial Trust which financed Industrial Research and Information Services which in turn produced an anti-militant trade union pamphlet. 'Charity May Face Tax Inquiry,' *Independent*, 3 February 1989.

government could afford to ignore.[37]

In lobbying the government, BP took advantage of a perceived split between Benn and the rest of the Cabinet. BP managers understand that several Labour ministers were moderates who could see the benefits to keeping BP as an independent company and maintaining the government's tradition of non-intervention.[38] These moderates included Prime Minister James Callaghan, Chancellor Denis Healey, Paymaster General Edmund Dell and the Dutchy of Lancaster Harold Lever. All were regarded as much more reasonable and balanced in their views than Benn.[39] One minister claimed he 'saved BP from Kearton,' the chairman of BNOC:

> [T]hough I was for a British owned oil company, I was not in favour of harming BP. It was a big successful company; it was nonsense to harm it. Therefore, I opposed it, and fortunately successfully.[40]

In 1976, the chairman of BP changed, and the new man, David Steel saw that in order not to jeopardize the Cabinet's support, it was essential for BP to be seen to be cooperating with the government. Even though BP was strongly opposed to the government's proposed participation policy for North Sea oil production, the company continued to put forward their best people in negotiations and worked hard preparing papers for discussion.[41] The government's desire to get an agreement from BP on participation was very strong, as it would set an important precedent for the rest of

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[37] Wyn Grant, 'Large Firms and Public Policy in Britain,' *Journal of Public Policy*, Vol.4, Fall 1984, pp.2-3.

[38] Interviews with Department of Energy civil servant, Labour ministers and BP executive.

[39] Interviews with BP executives.

[40] Interview with Labour minister.

[41] Interview with BP executives.

the companies operating in the North Sea. On this one issue the Cabinet did appear united, and BP perceived that it had become politically important for the Labour government to show progress on its energy policy.[42]

BP thus set its priorities and offered its cooperation on participation in exchange for the reduction of the government's shareholding. The link was made only at the highest level, between the Secretary of State for Energy, the Prime Minister, and the chairman and deputy chairman of BP; lower level managers did not know of these discussions.[43] Tony Benn records an evening at Chequers where the subject was discussed:

> Then we sat round the log fire with coffee, brandy and cigars and Harold Wilson said, 'We take no decisions at Chequers. This meeting didn't take place. Tony has explained your position but I didn't understand a word; will you tell me.' David Steel then launched into BP's objectives: independence, cash flow from the Forties Field, North Sea operations and international operations to be preserved. He said, 'The BP shares owned by the Bank of England are a problem. We can offer you help but no more.'[44]

Callaghan and Benn formally insisted, however, that the issues not be connected. Whether they were secretly linked or not, BP agreed to a final participation agreement in July 1976,[45] and five months later in December 1976 the government announced that it would reduce its holding from 68 per cent to 51 per cent, and the company's independence was thus maintained.

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[42] Interview with BP executives.

[43] Interview with BP executives.

[44] Benn, *Against the Tide*, p.506 another example on p.449; and confirmed by interview with BP executive.

[45] For BP agreement on participation see: 'Gulf Agrees to North Sea Share for State,' *Times*, 26 February 1976, p.1; and Roger Vielvoye, 'BP and Government Sign Wide-Ranging Deal on North Sea,' *Times*, 2 July 1976, p.21.

Government Could Not Come Up With the Cash

Changes in the structure of the international oil industry had caused BP to expand in new and costly ways, which forced the company by 1981 to raise additional cash from its shareholders. The company's financial health was threatened if its major shareholder was unable to meet the new demands placed on it. By 1980, BP needed to raise cash. The government, in fact, had always been a reluctant investor.[46] As one BP executive explained:

> There had always been a problem over the years. Whenever we wanted capital, it was always the wrong time to get it. The government would respond that they couldn't find the money this year, or could we do it some other way than effecting the government's shareholding, like convertible debentures.[47]

BP's cash needs arose after the flush period of the mid-1970s. Though BP's sources of crude oil were declining, profits increased through the 1970s with the price rises beginning in 1973-74. These profits provided the funding for BP's exploration in the North Sea and Alaska, as well as diversification through acquisition - both geographically, in terms of oil exploration, and also into new industries including chemicals and nutrition. The problem many BP managers argued was that BP paid too much for many of those acquisitions.[48] When the oil price dropped, the cost of exploration and production in the North Sea and Alaska remained high and the non-oil businesses were still not making a profit. Therefore, BP found itself in a position where its turnover continued to rise through 1985, but its profits declined steadily

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[46] Ferrier, *The History of the British Petroleum Company*, p.242 and pp.212-4.

[47] Interview with BP executive.

[48] Interview with BP executives.

(see Figure 5.3).[49] Beginning in the late 1970s, BP managers became concerned that although their resources exceeded their immediate requirements, the company had insufficient retained earnings to replace its diminishing reserves of crude oil.[50]

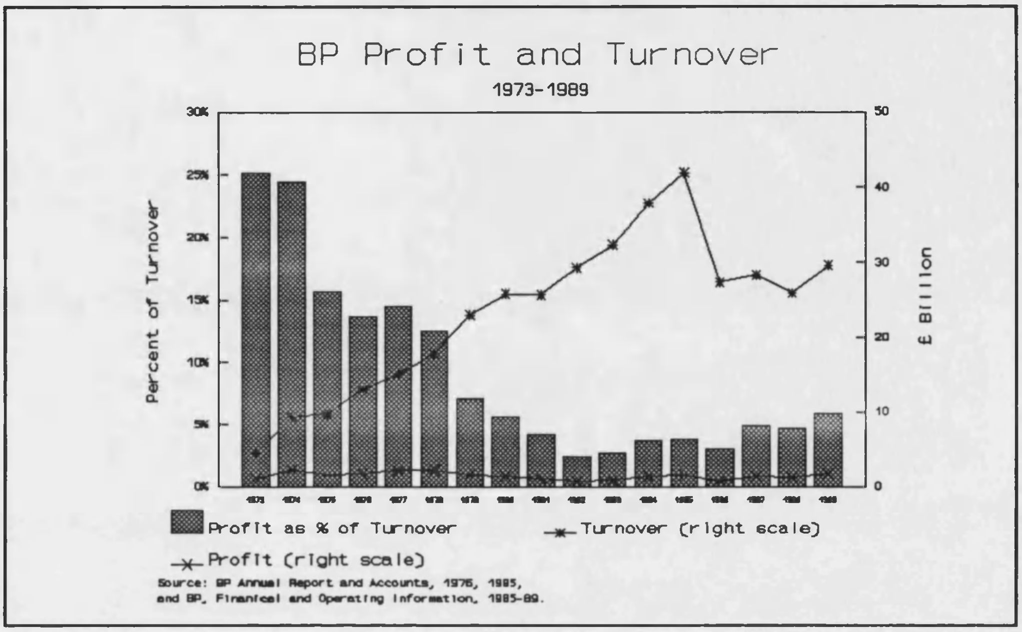

Figure 5.3.

Traditionally, BP's only other source of finance was from its shareholders. Because the government was reluctant to invest further, BP was forced into an uncomfortable position of turning to debt markets, selling subsidiaries or reducing growth.[51] The sheer size of the financial commitment to invest in further share offerings can in part explain the government's reluctance. The sums involved were vast. For example, BP's investment costs in 1983 worldwide were £2.8 billion and

[49] 'A Year of Frustrated Expectations,' *Petroleum Economist*, December 1982, p.482.

[50] 'Fifty Years of the Oil Industry,' *Petroleum Economist*, September 1983, p.327; Donald Croll, 'Focus on Upstream Operations,' *Petroleum Economist*, May 1984, p.169.

[51] Donald Croll, 'Finance and Investment,' *Petroleum Economist*, September 1983, p.333; Uwe Jahnke and P. Gordon Webb, 'A Bankers' View of Project Funding,' *Petroleum Economist*, October 1983, p.383; and 'Financing New Oil Production,' *Petroleum Economist*, May 1984, p.166.

in the North Sea alone, from BP's first investment in the late 1960s to 1984, BP spent £4.5 billion in the North Sea, paid £11 billion in taxes to the British government, and realised £7 billion in profits.[52] The cost to the government would have increased if they had enlarged their shareholding, unless the government chose not to subscribe in which case their percentage was diluted. The government's potential liabilities for BP's actual share issues in 1972 and 1981 for different percentage holdings are depicted in Table 5.2. The cost of nationalizing BP was not a one time expense of the acquisition of outstanding shares, but a continuous cost because the company required capital inputs to grow, as estimated in Table 5.2.

Table 5.2. Cost for Retaining Shareholding Percentage, Actual and Hypothetical, £ million

Actual	1972	1981
48%	36	---
46%	---	288
Hypothetical		
68%	51	424
100%	75	624

Source: BP, *Annual Report and Accounts*, 1972, p.29; and 1981, p.44.

The Costs of Government Ownership Overcame The Benefits

The benefits to government ownership, from BP's perspective, were primarily preferential treatment in the North Sea. The North Sea was very important to BP,

[52] 'Bringing in the Catch,' *Economist*, 12 May 1984.

more so than to the other major international oil companies. BP estimated that by 1980, 60 per cent of its UK sales came from the North Sea versus 20 per cent for Gulf, Shell and Exxon.[53] BP and Shell with their British ownership (Shell being 40 per cent British owned) proved to be the government's preferred choice for control of the North Sea.[54] However, when weighing the benefits, by the mid-1970s the BP management realized that the costs were clearly greater, especially as they realized that the benefits could be sustained without government ownership. The costs as previously mentioned were financial constraints and liabilities abroad.

BP's relationship with the government had become more complicated and different from when the government first invested in Anglo-Persian. When BP was operating abroad and repatriating profits back to Britain, the government benefitted from the inflow. In the North Sea, however, if BP diverted profits from the North Sea abroad, the government would realize an outflow of funds from Britain. BP's future depended upon building up world wide markets, and they therefore needed North Sea production revenues to meet their growing business abroad, especially Europe.[55] In contrast, the British government was less concerned with the companies' revenues than making sure that the oil was available for Britain.

The determining factor for the BP management, however, was the discovery of oil in Alaska and the growth of BP's markets abroad. British government ownership was a liability in the United States where there was a long history of

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[53] Interview with BP executive.

[54] Shell (a 60% Dutch, 40% British company) worked in partnership with the US company Exxon in the North Sea.

[55] BP, *Annual Report and Accounts*, 1980, 1989.

protected markets and favouritism for American producers. It was, therefore, difficult for BP, a British company, to enter the market and gain concessions to fields in Alaska. The United States government did not want BP exporting Alaskan oil to Britain (or anywhere) if a crisis should occur and there were oil shortages in the United States.[56] Even today, BP oil produced in Alaska cannot be exported.[57]

The shifting centre of BP's activities is evident from the statistics. By 1980, over 20 per cent of BP's crude oil production came from Britain and over 30 per cent came from the United States; by 1985, these proportions had reached 33 per cent and 59 per cent respectively. Britain had always been the largest source of crude oil sales, representing 57 per cent in 1980 and 52 per cent in 1985, but the importance of the United States grew rapidly during the late 1970s and early 1980s. The United States represented 25 per cent of sales in 1980 and 36 per cent by 1985.[58] While not determining factors, the management also saw a government share sale as a way to increase the number and geographical distribution of its shareholders, something they thought necessary for an international or 'stateless' company.[59]

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[56] Interview with BP executives, Treasury civil servant, CPRS official and Labour minister; Donald Croll, 'Marked Recovery for Most in 1987,' *Petroleum Economist*, June 1988, p.196; and BP *Annual Report and Accounts*, 1987 and 1988. Some in BP played this down, however, arguing it was over-stated in the UK. Interview with BP executive.

[57] Interview with BP executive.

[58] BP, *Annual Report and Accounts*, 1981 and 1989.

[59] Interview with BP executives. See discussion of 'stateless' companies in Wyn Grant, 'Economic Globalisation, Stateless Firms and International Governance,' University of Warwick, Department of Politics and International Studies, Working Paper No.105, April 1992; and William Holstein with Stanley Reed, Jonathan Kapstein, Todd Vogel and Joseph Weber, 'The Stateless Corporation,' *Business Week*, 14 May 1990, pp.52-9.

5.2. The British National Oil Company and the National Interest

By the early 1980s, BNOC was financially independent from the government and was grudgingly recognized as a success both in terms of profit and achieving national objectives. The management of BNOC was proud of both successes and by the early 1980s exceptionally loyal to the entity they had created. Though BNOC's credibility remained linked to government ownership, there was tension with ministers which heightened the management's desire for greater autonomy from government intervention. When the government proposed to split and sell only half of the company, however, the BNOC management was opposed, placing greater importance on the company than on the form of ownership. Because of BNOC's relatively small size and influence, they were limited in their ability to prevent the move.

Profit and Grudging Respect

Because BNOC's objectives for serving the national interest were not stated explicitly, it is hard to measure the company's success in those terms. In market terms, however, there is more concrete evidence. The management was able to raise funds from the private market beginning in 1977 with a loan of $825 million from a consortium of twelve UK and US banks, and expanded internationally (as discussed in Chapter Two). Most importantly, the company's finances were strong. The company's turnover increased from only £24 million in 1976 to over £9 billion in 1984, and was making a healthy profit of over £21 million by 1979 and £88 million in 1980. In 1981, however, Britoil was separated from BNOC, and the profits of the company were drastically reduced (see Table 5.3).

In 1979, the new Conservative government eliminated BNOC's special

Table 5.3. BNOC Accounts		
	Turnover £ mil	Net Profit (Loss) £ mil
1976	24	(2)
1977	28	(2)
1978	432	(3)
1979	3,245	22
1980	4,323	88
1981	5,752	77
1982	6,465	58
1983	7,910	0
1984	9,562	(12)
Source: BNOC, *Annual Report and Accounts*, 1976-1984.		

privileges including access to the National Oil Account, the right to sit on all operating committees, exemption from paying Petroleum Revenue Tax, the right of first refusal on all leases changing hands, and the right to 51 per cent of all new licenses. The private oil companies operating in the North Sea had treated BNOC with contempt and suspicion because of these privileges.[60] Because the privileges were seen as politically imposed liabilities rather than privileges, their elimination was a boost to BNOC's commercial image. One BNOC executive explained: 'We were heartily thankful. I was delighted because we didn't want all of those political duties.'[61] Those in the DEn though saw it as a reduction of BNOC's power. One

[60] Roger Vielvoye, 'Exxon Chairman Says Group Not Volunteering for State Participation,' *Times*, 3 March, 1976, p.17; and 'Putting in Their Oar,' *Economist*, 2 June 1982, p.S16.

[61] Interview with BNOC executive.

Department of Energy civil servant stated: 'It was a "body blow" to BNOC; they saw that their special position would be eroded.'[62]

BNOC also co-operated when the government encouraged BNOC to sell exploration acreage and to license new developments in existing fields to other operators. Since BNOC was only three years old at the time, the creation of a Labour government and not well connected in the Conservative party, its management was tentative over its future and thought this might be a means to appease the Conservatives, heading off moves to split the company or sell more valuable assets.[63]

Serving the National Interest

The managers of BNOC were committed to their company and excited by BNOC's potential ability to serve the country which they felt they could do better than any other organization. There were many references to BNOC's expertise versus the government's lack of understanding. Sir Alistar Morton argued:

> BNOC could have developed the whole North Sea, and cost was not the problem. BNOC had no problem raising the funds in 1977, and could have done this on a much bigger scale, five to ten times larger. At the time $820 million could be paid back by one BNOC well [off-shore oil field] in four to five years. $820 million is now equal to $4 billion. What was missing from government, and always is, was vision or purpose.[64]

In many cases, the BNOC management argued that they could serve the national

[62] Interviews with Department of Energy civil servant and BNOC executive.

[63] Interview with Sir Alistar Morton, 15 October 1993, and interview with BNOC executive.

[64] Interview with Sir Alistar Morton, 15 October 1993.

interest better than the government. For example, in terms of the minimum percentage of North Sea oil required to be refined in Britain, one BNOC executive explained:

> The percentage that could go through the UK was larger than the [oil] industry had persuaded the Department of Energy it could be. BNOC's conviction was stronger than the department's. BNOC regularly surpassed the percentage requirements.[65]

Two of BNOC's objectives were often in conflict - supplying oil to Britain in a crisis was not always compatible with maintaining a stable oil price. In order to set the price of oil, or at least strongly influenced the price in the short-term, BNOC used contracts agreed quarterly or longer.[66] The use of long-term contracts compromised BNOC's ability to supply oil to Britain quickly. The 1979 oil crisis was BNOC's only real test, and (as described in Chapter Two) the business contracts that it had made, meant that BNOC could not shift the oil immediately.[67] In addition, honouring a preset price, even when short-term oil prices were falling, BNOC was forced into a loss-making situation. The management fought to end long-term contracts in favour of the current business practice of short-term or spot market purchases, but despite their arguments and substantial losses, the government required the continuation of long-term contracts.[68] The primary explanation for the

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[65] Interview with BNOC executive.

[66] Interview with BNOC executives; Richard Bailey, 'Unequal Shares in the North Sea,' p.2 and p.4; Zuhayr Mikdashi, *Transnational Oil Issues, Policies and Perspectives* (London: Francis Pinter Publishers, 1986), p.35 and p.71; 'Good Year for State Oil Companies,' *Petroleum Economist*, June 1982, p.253; 'Britain's Oil Policy,' *Petroleum Economist*, April 1984, p.123; and *Hansard Parliamentary Debates (Commons)*, 13 March 1985, vol.75, col.305.

[67] Interview with BNOC executive; *Hansard Parliamentary Debates (Commons)*, 14 May 1985, vol.79, col.254.

[68] *Hansard Parliamentary Debates (Commons)*, 14 May 1985, vol.79, col.203-4.

government's resistance was financial. Because the price set by BNOC was the price the government used as a tax reference point, the higher BNOC's price in a declining market, the less the government lost in terms of taxes. And the more stable BNOC's prices, the better the government could predict its oil revenues.[69]

The BNOC executives envisioned a larger role for themselves, but one that depended on governmental support. As part of their justification for remaining a whole company in government ownership, the management tried to convince the government of the importance of its potential role. As one BNOC executive explained:

> There could develop the situation where the North Sea was not attractive and [the private oil companies] would move elsewhere. At that time, the government would need a competent British company whose first priority was to develop North Sea oil in the interest of Britain as distinct from any commercial interest. Commercial and national interests may diverge.[70]

Because the government had explicitly ensured that daily revenues were deposited in the National Oil Account, BNOC had no way of retaining funds to develop the company infrastructure necessary for such non-commercial growth.[71] To institute this new objective, BNOC was dependent on government backing. From the beginning, finance was an important aspect of the company, and Treasury funds were made available only to meet BNOC's most basic development needs. In fact, as one Department of Energy civil servant remarked: '[The] Treasury's real concern, once BNOC was established, was that it would not represent an additional burden to the

[69] Interview with BNOC executive; and Alick Buchanan-Smith, Minister of State for Energy, *Hansard Parliamentary Debates (Commons)*, 18 December 1984, col.234.

[70] Interview with BNOC executive.

[71] Interviews with BNOC executives.

PSBR.' For example, there were no funds available for BNOC to expand to the refinery stage as intended from their original business plan.[72]

The management of BNOC was quick to point out the power BNOC had. Sir Alistar Morton explained:

> BNOC decided who got the oil and for how long. The price was set by the world market, but the power was in who received the oil and for how long. This was a great bargaining advantage for BNOC and the UK.[73]

He gave several examples of how BNOC used this advantage to serve Britain. These included how he negotiated a favourable contract with Germany to calm threats about going to the EC to settle the question of sovereignty over the North Sea; developed plans to convince all companies to explore west of the Shetland Islands, and aided British Airways during the 1979-80 oil crisis.[74]

Other BNOC executives also mentioned services BNOC provided. In the late 1970s, ministers requested three times that BNOC place orders for drilling rigs on Clydeside yards, but BNOC was not sure they could buy the rigs and sell them at a profit. BNOC therefore requested an official direction from the Secretary of State for Energy before fulfilling the order.[75] In another case, BNOC served the government's development needs by moving BNOC headquarters, in a controversial decision, to

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[72] Interview with BNOC executive; House of Commons Nationalized Industries Select Committee, 'Testimony by Frank Kearton, Chairman of BNOC,' p.2; and Peter D. Cameron, *Property Rights and Sovereign Rights: The Case of North Sea Oil* (London: Academic Press, 1983), p.158.

[73] Interview with Sir Alistar Morton, 15 October 1993.

[74] Interview with Sir Alistar Morton, 15 October 1993.

[75] Interviews with BNOC executives; and Department of Energy, 'About Britoil,' p.10.

Glasgow instead of Aberdeen.[76] Possibly the most important event for the functioning of the business though was when BNOC's needs were deferred to the government's financial needs and the development of the Clyde oil field was delayed for three years in the mid-1980s.[77]

BNOC also arranged forward oil sales in 1980 and 1981 which enabled the government to record the revenues one year in advance, to meet the government's short-term financial objectives.[78] Sir Alistar Morton explains how these sales came about:

> In the summer of 1979 the government came to BNOC and told us that they were £500 million short, could we sell something, were any fields worth £450-£500 million? We responded by asking, if we can raise the money another way, can we avoid breaking up BNOC? We knew that once the government started [selling off BNOC] they would't stop.The concept of a forward sale of oil confounded them, but to us, it was old hat, we had raised $820 million in 1977 in that way. The government thought it would take us six months, the sale of an oil field would have taken that long, but it only took us 17 days to raise £620 million.[79]

BNOC was able to raise £620 million in this way to credit the 1979/80 PSBR. The following year, BNOC again sold oil forward, this time raising £550 million to credit to the 1980/81 PSBR.[80] Morton went on to add his disdain for the government's lack of understanding about the power of oil: 'Oil was valuable, but the government did

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[76] John McCall, 'The Lawyer's Role in the Oil Industry - A Look at the British National Oil Corporation and its Legal Department,'*International Business Lawyer*, Vol.7 (iii), 1979, p.146; and interview with BNOC executive.

[77] Interviews with BNOC executives; and Martin Quinlan, 'The Need for New Oil,' *Petroleum Economist*, June 1981, pp.249-50.

[78] Interview with BNOC executive.

[79] Interview with Sir Alistar Morton, 15 October 1993.

[80] *Hansard Parliamentary Debates (Lords)*, 9 October 1980, vol.413, col.708-710; Redwood, p.109; and 'BNOC: Up for Grabs,' *Economist*, 4 October 1980, p.63.

not recognize it. The whole thing bedazzled them.'[81]

The Management's Dilemma

With the prospect of privatization, the BNOC management was forced to decide and defend its ownership preference. While government ownership was not obviously important, keeping the company whole and retaining the right to fulfil their original mission was (see discussion in Chapter Three). All of the executives and board members who I interviewed expressed a sense of accomplishment and pride. They were attached to the business they had helped create and were determined to defend its future. The reasons why they joined BNOC and why they wanted it to continue varied, however, from nationalist to commercial arguments.[82] BNOC was described as 'a great opportunity' and a chance 'to get in on the ground floor of something interesting and new.'[83] One former civil servant joined because he was worried about his finances and could earn more at BNOC than in the civil service.[84] Others had enjoyed working with Kearton previously and were persuaded by him to join BNOC.[85]

The one thing they did have in common, a BNOC executive explained, was that 'most employees had a belief in the need for BNOC; they identified with it, and

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[81] Interview with Sir Alistar Morton, 15 October 1993.

[82] Interviews with BNOC executives; and House of Commons Nationalized Industries Select Committee, 'Testimony by Frank Kearton, Chairman of BNOC,' p.56.

[83] Interviews with BNOC executives.

[84] Interview with BNOC executive.

[85] Interview with BNOC executive.

they had strong motivations.'[86] The new chairman Frank Kearton believed that the state should participate in the advantages of North Sea oil, but also believed these assets should be controlled by a commercially run entity.[87] A few of the early board members, however, were committed to the ideology of state owned industries. By the time Kearton retired in 1979, the remaining members were predominately business oriented, with some degree of regard for the national interest.[88] One BNOC executive claimed:

> I actually got more kick from believing that I was doing something which was in the community's interest...than I got from the salary.[89]

Sir Alistar Morton summarized the position of most managers: 'BNOC was capitalist, but not Thatcherite. We all strongly believed that the UK should have a state oil company, and BNOC proved this in many ways.'[90]

The management's strategy to prevent a change was to delay the government's moves towards a sale. As one BNOC explained:

> We made sure that they [the Conservatives] were aware of all the complications, legal implications with the joint ventures, international markets etc. ..by the time we finished with them, they were really confused. We thought that the Conservative's desire [to sell BNOC] would pass, so delaying tactics were best.[91]

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[86] Interview with BNOC executive.

[87] Interviews with BNOC executives.

[88] Thomas Balogh was Member of the Economic and Financial Committee of the Labour Party, 1943-64 and 1971-85; Minister of State in the Department of Energy, 1974-75; and Deputy Chairman, BNOC, 1976-78, and economic advisor, 1978-79. Interviews with BNOC executives.

[89] Interview with BNOC executive.

[90] Interview with Sir Alistar Morton, 15 October 1993.

[91] Interview with BNOC executive.

The commitment of the management to the company was an important factor in all of the asset sales but the government's ability to appoint a new chairman, negated the power of this factor in the case of BNOC. It was apparent that the Conservative's choice, Philip Shelbourne, was committed to privatization, but even he was not enthusiastic about the idea of splitting BNOC.[92] But since his loyalty was to the government, he took on the task of convincing the board to accept the government's decision even though they were strongly opposed.[93]

For the personnel of BNOC in 1981, the split and the sale meant that all operations stayed intact, but separately. Britoil became a private sector company, with Shelbourne as its chairman, and BNOC remained an oil trading operation headed by the then deputy chairman Lord Croham. Those who went with Britoil were reluctant because, as one BNOC executive said: 'I would have liked to stay with BNOC, but didn't think it was viable.'[94] They were persuaded that they might still be able to serve the national interest by further developing the North Sea, and only one executive resigned when Shelbourne was appointed, which by all accounts was for personal reasons.[95] In fact, the management of Britoil continued many of BNOC's practices which were oriented towards serving Britain's interest, such as focusing on exploration in the North Sea. Some argued that this was to the detriment of Britoil's

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[92] Interviews with BNOC executives.

[93] Interviews with BNOC executives; Hugh Stephenson, 'A Dreadful Waste of Energy,' *Times*, 17 June 1980, p.19; and Cameron, *Property Rights and Sovereign Rights*, p.168.

[94] Interview with BNOC executive.

[95] Alistar Morton and Philip Shelbourne had had a falling out years earlier when they were both working for merchant banks. Peter Hill and Richard Evans, 'Top Executive Resigns from BNOC,' *Times*, 31 May 80, p.19.

future and one of the reasons why the company was such an easy takeover target.[96]

For those in the trading operation, prospects were not as good. Though Ian Goskirk, a dynamic oil executive, remained to head the trading operations, it was clear that BNOC's days of controlling the majority of North Sea oil were over. Once the government's plans of splitting the company were confirmed, two senior officials in the trading operation resigned to return to the private sector.[97] One executive who stayed with BNOC confessed:

> I would have preferred to go to Britoil, I was more interested in physical operations than trading operation. I had only planned to work for 5 years after retirement from civil service anyway.[98]

Another recognized the limitations the split imposed for the career opportunities for younger employees as previously there had been much back and forth between the production and trading operation that would no longer be possible.[99] Ultimately the remaining trading operations of BNOC were wound down in 1985 and Britoil was taken over by BP in 1988, thus confirming the management's initial fears in 1980.

5.3. British Gas Corporation: Defending Its Empire

By the early 1980s, BGC had proved not only that it was financially successful, but that it was a strong and independent company finding and providing gas efficiently to British customers. As such, the management was proud of what it had achieved, but as a large, long established and successful company also had

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[96] Interview with BNOC executive.

[97] Ray Dafter, 'Two Senior Officials Resign from BNOC,' *Financial Times*, 25 February 1982.

[98] Interview with BNOC executive.

[99] Interview with BNOC executive.

important resources to defend its interests, which it chose to use in the face of the government's plans to disassemble and sell its oil assets.

Independence and Success

BGC became financially independent by 1980: It was greatly aided by the discovery of gas in the North Sea, and also by the structure of the company as defined in the 1972 Gas Act and its monopoly power. One of the crucial clauses in the Act prevented the government from directly taking the profits from British Gas (as it could do with BNOC). When the Gas Act was written in 1972, the corporation was small and only limited quantities of gas had been brought ashore from the North Sea. The financial legislation, therefore, focused on borrowing requirements and assistance, not on profits and profit retention. While the Secretary of State was given the authority to withdraw excess revenues (should there be any in the future), there was a caveat that became important later. The Secretary of State could have excess revenues paid to him, provided:

> that no such direction shall be given as respects any financial year unless the total of the sums standing to the credit of the Corporation's reserves at the beginning of that year exceeds 10 per cent of the value at the beginning of that year of their net assets as for the time being defined for the purposes of this section by the Secretary of State.[100]

In practice, this meant that the government could only extract profits after British Gas had made provisions to build adequate reserves.[101] The finance

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[100] Gas Act of 1972.

[101] British Gas Corporation, 'The Work of the Financial Division,' internal memo, early 1980s, p.2; and William Jewers, 'Required Rate of Return, Test Discount Rate, Pricing Policies and Financial Targets,' Seminar on the Financial Target of Public Corporations, 30 January 1979, p.2.

managers of British Gas acknowledged that the amounts necessary to replace existing assets were not easy to determine, especially during periods of high inflation. The problem was that existing reserves had to be replaced at current prices rather than historic costs. Officially, the rates of depreciation, as well as BGC's financial targets, were set by the Ministry of Trade and Industry and later the Department of Energy, in consultation with BGC. As the main provider of information, the management, however, was very influential. They convincingly argued that savings based on historic cost alone would oblige British Gas to borrow money to meet current costs just to maintain the business in its existing state, potentially creating an interest charge burden that BGC could not support.[102] One BGC finance executive argued that it was his responsibility to ensure that the replacement of existing assets at current cost was met from current revenues.[103] BGC also had (or created) room to manipulate the accounts to protect its own interests. For example, two measures were introduced in the mid-1970s which increased the amount of revenues set aside for building reserves, and also had the effect of keeping profits down. In the 1976-77 fiscal year, BGC introduced a supplementary depreciation charge into the revenue account to provide for the current replacement cost of assets, and from the 1975-76 fiscal year BGC charged certain day to day items of replacement expenditure to revenue.[104]

By the early 1980s BGC began to assert its independence more and its

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[102] BGC, 'The Work of the Financial Division,' p.5; and Jewers, 'We're Not As Different as Private Industry Thinks,' pp.330-1. This was a generally accepted characteristic of BGC, see Lynn Pearson, *Organization of the Energy Industry*, p.100.

[103] Jewers, 'Required Rate of Return,' p.8.

[104] BGC, 'The Work of the Financial Division,' p.5; and Jewers, 'We're Not As Different as Private Industry Thinks,' p.332.

management became adamant that they and not ministers should run the business. Even though the government had the power to set the financial targets in consultation with BGC, in 1980 the chairman Denis Rooke wrote to David Howell, the Secretary of State for Energy, and argued that he did not agree with his financial targets. According to a BGC executive, Rooke said that the gas industry was his industry, not the government's, and BGC should, therefore, be setting the financial targets.[105] The government ultimately had the final say. For example, in 1984 BGC wanted to expand internationally by purchasing gas from Norway's Sleipner field. In the company's view this step was consistent with serving its customers and preserving the future of the business. Access to the enormous Sleipner field would have ensured adequate long-term supplies. Christopher Brierley, Head of Economic Planning, explained: 'British Gas cannot gamble with its customers' supplies.'[106] In February 1985, ministers rejected the proposal because they wanted to ensure that gas resources in Britain were developed. BGC managers were deeply disappointed and resentful of the government's interference.[107]

BGC also gained some independence by increasing its private sector operations. In 1976-77, BGC was granted permission to operate in the commercial market.[108] Given the valuable assets the company had developed, the private sector

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[105] Interview with BGC executives.

[106] Martin Quinlan, 'British Gas Stresses Need for Imports,' *Petroleum Economist*, December 1984, p.445.

[107] Martin Quinlan, 'British Gas Stresses Need for Imports,' *Petroleum Economist*, December 1984, p.445; and 'Sleipner Cancellation Boosts UK North Sea,' *Petroleum Economist*, March 1985, p.84.

[108] Pearson, *Organization of the Energy Industry*, p.100.

was willing to finance most of its needs.[109] BGC worked to increase its production as well as the number of supply contracts with private companies. As a consequence, it was necessary for BGC to follow current business practices so that private companies could better evaluate the corporation, which forced BGC to act more like a private company. This strong business attitude was welcomed by the Treasury, which BGC saw as an ally. As was the case for BP and BNOC, the management of BGC perceived that the Treasury supported their business success. As one executive explained, 'what was good for BGC was good for Treasury. BGC profits meant a better PSBR for the Treasury.'[110]

Being a monopoly in the gas industry, the corporation took advantage of the power, but being government owned was also subjected to political intervention. For example, in 1976 the government imposed an increase in the price of gas not because the industry required it, but for political reasons, to help offset the rising PSBR.[111] Though oil was not the corporation's core business, the management feared that the oil asset sales were another means for the government to interfere, they were especially worried because the measures could set a precedent for the rest of their business.[112]

BGC's position was also weakened because its financial success (linked to the 1972 Gas Act structure) became too conspicuous. By 1981 not only had BGC repaid its loans to the government, it started lending money (£200 million in 1979 and

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[109] BGC, *Annual Report and Accounts*, 1985.

[110] Interview with BGC executive.

[111] Interview with BGC executive; and 'Large Rise in Gas Prices,' *Petroleum Economist*, 19 February 1980, p.80.

[112] Interviews with BGC executives.

another £100 million in 1980) to the government under a 'reverse' National Loans Fund arrangement with an interest rate agreed between the Treasury and BGC, approximately two points below the going rate.[113] The government also developed means to extract extra revenue from BGC through taxes and levies. BGC went from paying £184.8 million to the government in taxes and royalties in the 1979-80 fiscal year and £87.6 million in 1980-81 (in addition to the loans in both years) to £1 billion in 1982-83 (when no further loans were made). The tax bills declined slightly in the following years but only to £704.9 million in 1984-85. At the same time, however, the government received the £392.2 million proceeds from the sale of BGC's offshore oil assets.[114]

Illustrating the corporation's political power, instead of accepting the tax increase quietly, the company passed them on to customers and enclosed a leaflet with every household gas bill which effectively blamed the government for the rise in prices. Conservative Members of Parliament were inundated with complaints from constituents who held the government responsible.[115] BGC's strong public campaign demonstrated its corporate emphasis upon autonomy and its readiness to exploit available resources actively to contain adverse policy shifts by ministers.

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[113] BGC, *Annual Report and Accounts*, 1981 and 1985; and Jewers, 'We're Not As Different as Private Industry Thinks,' p.330-1; and interview with BGC executive.

[114] BGC, *Annual Report and Accounts*, 1981-85; and Enterprise Oil, 'Offer for Sale,' p.iii. The tax figures exclude VAT and PAYE.

[115] Lawson, *The View from No.11*, p.172; and interview with Department of Energy civil servant; Ian Glover-James, 'Gas Price Row is Cooled,' *Daily Telegraph*, 31 July 1981, p.2; and 'Large Rise in Gas Prices,' *Petroleum Economist*, 19 February 1980, p.80.

The Management's Commitment to its Corporation

The BGC management was loyal, proud of the corporation, and resented government interference. Many of the executives had the choice of working for either a private sector company or BGC and chose BGC despite the lower pay. They were rewarded with a sense of accomplishment in building up an organization they saw as a national asset.[116] As a whole, one BGC executive explained, BGC was a valuable British resource:

> Britain is fighting an economic war against the rest of the world. BGC is a little bit of it with international obligations. Rather than try and carve everything up in Britain and make every man at every level compete with his brother, what you [the government] should be doing is try to build up a number of significant lead industries in Britain which are important to the core industry and strong enough to be independent and fly world wide. What you should be doing is to reinforce success where you find it, because there is too little of it in Britain. What you are doing is carving up companies whether they are successful or not, just on some theoretical model.[117]

Like BNOC, the management opposed any division of their corporation. The BGC management argued that selling discrete pieces such as its oil assets would undermine their ability to serve the national interest. The 1980-81 *Annual Report* stated: 'The corporation believes that disposal [of the oil fields] would impede or prevent the proper discharge of its statutory duties.'[118] The pride managers felt in their achievement made them adamant that none of BGC's operations should be destroyed or diminished.[119] Managers also had less noble reasons, such as benefits

[116] Interview with BGC executives and Department of Energy civil servant.

[117] Interview with BGC executive.

[118] BGC, *Annual Report and Accounts*, 1980-81, p.10.

[119] Interview with BGC executives their personal views as well as an assessment of the Board and BGC employees.

that stemmed from being employed in a lucrative monopoly. BGC's offices were plush and there were non-salary benefits such as daily chauffeur transportation to and from work for top level executives.[120] As one civil servant surmised: 'Profits were part passed on to customers in cheap prices, part to government and part BGC spent on extravagances.'[121]

The management's commitment to preserving the whole company intact, for national service or personal perks reasons, is evident from the corporation's flat refusal to sell any of its assets unless ordered to do so. The issue of selling its oil assets first arose in 1975 when the Labour government's original plans for BNOC included transferring the oil assets from the National Coal Board (NCB) and BGC to the new national oil company.[122] BGC, however, fought the sequestration by arguing that it was difficult to distinguish between oil and gas fields before they were developed.[123] When BNOC was created in 1976, very few of BGC's fields had been developed. By the early 1980s, however, these arguments no longer held. Most of BGC's fields had been explored and were producing, making it obvious which were gas and which were oil fields. At the same time, the general relationship between BGC and the government had changed too. In the mid-1970s, BGC was still repaying loans to the government, by the early 1980s, BGC was highly profitable and was

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[120] Interview with BGC executive and Treasury civil servant.

[121] Interview with Department of Energy civil servant.

[122] On 28 February 1975, John Smith, MP, Parliamentary Secretary in the Department of Energy announced that the assets of the NCB and British Gas would form the basis of BNOC. Gerry Corti and Frank Frazer, *The Nation's Oil: A Story of Control* (London: Graham & Trotman, 1983), p.104.

[123] Interview with BGC executive and Department of Energy civil servant.

loaning money to the government.[124]

Using its corporate expertise and well established government contacts, the BGC management was able to resist implementation of the government's plans. One DEn civil servants stated: 'I thought Rooke was as obstructive as he could decently be. Other people thought he was indecent.'[125] The management used all available means to block the sale including lobbying Members of Parliament, giving information to members of the opposition parties who then called for hearings and investigations, and arguing over the value of the field itself. The management argued that the bids were not high enough and delayed the negotiations. They even tried to retain a small shareholding, without success.

The implications for delaying the sale were significant as illustrated with the Enterprise Oil sale. The timing of the 1983 election meant that the Secretary of State for Energy Nigel Lawson almost failed to implement the sale of Enterprise Oil. As Lawson explained,

> I was just about to sign the instruction to [Rooke]...when the 1983 election was called. Constitutional propriety required that any further action be delayed until the outcome of the election was known.[126]

Had Labour won, or even a more sympathetic Conservative minister replaced Lawson after the election, BGC might not have been forced to sell its oil assets. In fact, the new Secretary of State Peter Walker later proved to be more sympathetic towards BGC. Lawson, however, was determined that only a (highly improbable) Labour victory should thwart the sale. He signed a letter to enact the disposal before leaving

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[124] BGC, *Annual Report and Accounts*, 1979-1983.

[125] Interview with Department of Energy civil servant.

[126] Lawson, *The View from No.11*, p.215.

for the campaign trail, and gave it to his private secretary for safekeeping with instructions to destroy it if the Conservatives lost the election, but to send it on upon receipt of a telephone call if they won. Lawson telephoned the day after the election, and the letter was sent. It turned out to be Lawson's last act as Energy Secretary before becoming Chancellor of the Exchequer.[127] It seems that the Cabinet Secretary, Robert Armstrong, looked the other way at this breach of previous convention.

In BGC's case, ministers did not take advantage of the end of the chairman's term to replace Denis Rooke, a very vocal opponent of privatization. When his first term ended in 1980, David Howell reappointed Rooke. Some Department of Energy civil servants thought that Howell was intimidated by Rooke and was too frightened of making waves not to reappoint him.[128] Lord Lawson's hindsight view, however, was that there was no reason to replace him:

> Howell was not yet thinking about the privatization. The only thing that was being discussed for sale at the time was the BGC showrooms which were introduced by the Department of Trade and Industry (DTI) in response to a poor report on competition policy.[129]

When Lawson became Secretary of State for Energy, he could not fire Rooke. But he could and did appoint new board members to minimize Rooke's power and increase Lawson's information about BGC.[130]

Ultimately, BGC's management could not prevent the sale of their assets, and

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[127] Lawson, *The View from No.11*, p.215.

[128] Interview with Department of Energy civil servant.

[129] Interview with Lord Nigel Lawson, 15 February 1994.

[130] Lawson, *The View from No.11*, p.214.

thus the sale proceeded, raising £215 million which was retained by BGC.[131] The matter of retaining the proceeds was not the key point of conflict, however. In fact, BGC management had demonstrated its preference was to keep the assets. When the government announced its intention to separate and sell the oil assets of BGC in 1980, but before any concrete plans had been made, Rooke was approached by the chairman of RTZ Alistar Frame who wanted to buy BGC's offshore oil assets. Even though BGC could have received the proceeds from a sale to RTZ, Rooke refused and the board backed his decision.[132] Shortly thereafter, the government passed the 1981 Oil and Gas (Enterprise) Act which gave the Secretary of State for Energy the authority to direct BGC to separate and sell its oil fields and directed the proceeds to the Treasury instead of BGC.

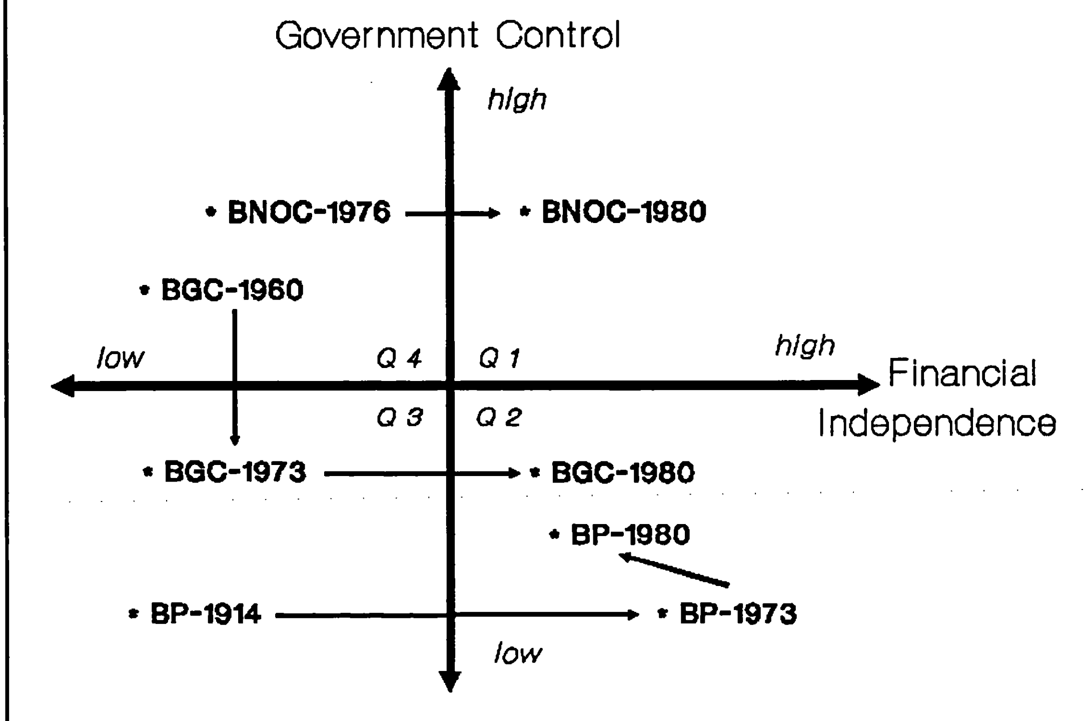
Conclusion

The variations in the three companies' reactions to privatization clearly reflect their different situations in terms of the three variables outlined above: organizational autonomy, financial independence, and success in achieving the company's mission. The different situations of the companies in terms of organizational autonomy and financial independence are illustrated in Figure 5.4. BNOC started in 1976 as a company with a large amount of government control and little financial independence (quadrant 4). After obtaining finance in the private sector and increasing the size of its production and trading operations by 1980, BNOC became financially independent,

[131] BGC, *Annual Report and Accounts*, 1983-84, p.5; and BGC, 'Report to Employees,' 1981-82.

[132] Interview with business executive and BGC executive.

Figure 5.4. Company Status: BNOC, BGC and BP



but because of the government's narrow legislation remained under government control (quadrant 1).

BGC was a financially unsuccessful company controlled by the government (quadrant 4) until 1972 when its governmental control mechanisms were re-written with the 1972 Gas Act, it then became more autonomous (quadrant 3). After its North Sea fields began to produce, BGC's position shifted again to one that was more financially independent (quadrant 2). As government ministers sought new means to assert control over the company and capture the company's increased profits, BGC managers sought to preserve their autonomy and independence (i.e. fearing a return to quadrant 4).

When the government first invested in BP in 1914, it was because BP was in need of financial assistance. But the financial dependence did not mean a loss of organizational autonomy as the government agreed to a non-intervention arrangement (quadrant 3). With its exploration and production success in the Middle East, BP became financially independent and became increasingly so with the oil price rises in the mid-1970s (quadrant 2). When BP faced cash shortages and turned to its shareholders, managers feared a return to financial dependence on the government (quadrant 3) and thus sought alternative means to maintain its independence.

Generalizing these findings, companies in quadrant 2 are the most receptive to privatization and are the best able to influence the outcome. Companies in quadrant 1 and 3 have mixed preferences towards privatization and are less effective in demanding their preferences. Finally, managers of companies in quadrant 4 are resistant to privatization and such companies are the most difficult to transfer to the private sector.

A company's mission becomes important for privatization implications when a company has low autonomy in which case the company has a profit motive and the managers will be more enthusiastic for the company to be privatized than they would if the company had a national interest mission. The one exception is a company that has successfully achieved its mission, either high profits or good national service, and needs to be split in order to be sold. In such cases, the management will desire government ownership of the whole company over greater autonomy or independence. Because the companies in this case were all successful in achieving their missions, the managers were attached, loyal and protective of their respective companies. For the managers of BP, this was not an important factor as the company was already autonomous and independent and had a profit motive - and the government did not consider splitting BP. Privatization of BNOC and BGC's oil assets, however, entailed splitting the companies and therefore the managers resisted the privatization measures, making privatization more difficult.

The ability of the managers of each company to resist was a product of the financial independence and their success in achieving their mission. Because BP was the most autonomous, financially independent and successful in achieving its profit mission, its managers were the most effective in keeping their company whole and maintaining their autonomy. Because BGC was autonomous and financially independent yet still susceptible to government interference, its managers were only able to delay the sale of the company's oil assets. Finally, because BNOC was not autonomous despite being financially independent, its managers were the least successful in maintaining the company as a whole. BNOC managers efforts to delay or prevent the split of its company and privatization were thwarted by the government's appointment of a chairman favourable to privatization.

Chapter Six: Public Choice and the Government Bureaucracy

Budget-maximizing theories assume (mostly from American experience) that bureaucrats not only want the power and status that comes with bigger governmental departments, but the pecuniary benefits that come through bigger budgets. The theory predicts that bureaucrats always demand bigger budgets and search for new means to create bigger departments.[1] In the post war period, departmental budgets have mostly grown, providing some prima facie evidence that these assumptions could be correct. Applying the conventional expansionist model to a government's sale of assets, we would expect civil servants to resist any reduction of their department's size, yet I found the exact opposite. The civil servants in the British government provided no opposition to the government's oil asset sales and in several cases aided the process. More recent work in public choice suggests some explanations. First, recent empirical studies have argued that the link between budget growth and pecuniary benefits is weak if it exists at all.[2] Second, studies have questioned the traditional assumptions

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[1] Niskanen, *Bureaucracy and Representative Government*, p.38; Robert Goodin, 'Rational Politicians and Rational Bureaucrats in Washington and Whitehall,' *Public Administration*, Vol.60, Spring 1982; James Buchanan and Geoffrey Brennan as interpreted in Richard McKenzie and Dwight Lee, *Quicksilver Capital: How the Rapid Movement of Wealth had Changed the World* (New York: The Free Press, 1991), p.29; Dennis Mueller, *Public Choice II* (Cambridge: Cambridge University Press, 1989), Chapters 3, 17, 23 and 24; Sam Peltzman, 'The Growth of Government,' *Journal of Law and Economics*, Vol.23, No.2, October 1980, pp.209-18; and A.H. Melzer and S.F. Richard, 'Why Government Grows, and Grows, in a Democracy,' *Public Interest*, Vol.52, Summer 1978, pp.111-18.

[2] For example, Ronald Johnson and Gary Libecap ('Agency Growth') provide evidence to show: 'At best, agency size would have to double for salaries to increase by 4.4 percent over a five-year period.' (p.448); also see Robert Young, 'Budget Size and Bureaucratic Careers,' pp.36-43; a study by Keith Roberson as described in Douglas Wass, 'The Public Service in Modern Society,' *Public Administration*, Vol.61, Spring 1983; and Sophie Watson, 'Is Sir Humphrey Dead? The Changing Culture of the Civil Service,' Working Paper 103, University of Bristol, School for Advanced Urban Studies, July 1992, p.60.

Yet Andrew Dunsire shows evidence that staff cuts in the British civil service from 1980 to 1984 of 8% produced a 5% salary increase. Andrew Dunsire, 'Bureaucrats and about bureaucrats' motivations. For example, Dunleavy's 'bureau shaping' model argues that

> higher-ranking bureaucrats place more emphasis upon non-pecuniary utilities: such as status, prestige, patronage and influence, and most especially the interest and importance of their work tasks.[3]

Accepting the importance of non-pecuniary motivations makes it possible to understand instances where it is in the interest of civil servants to reduce the size of their departments or of the government apparatus in general. Dunleavy argues that bureaucrats collectively pursue such strategies when greater power or job satisfaction can be achieved as a result.[4]

To fully understand different bureaucrats' actions, in addition to motivations, we also need to recognize the different constraints faced by bureaucrats. Until recently, the importance of the institutional structures in which actors work has not been fully recognized. The work in the field of the 'new institutionalism' can be seen as a reaction to the lack of attention scholars have paid to constraints.[5] Evidence

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Conservative Governments,' in Blais and Dion, eds., *The Budget-Maximizing Bureaucrat*, pp.192-4. Dunsire has merely shown a correlation, though. A more likely explanation for the salary increases was the Conservative electoral promises to honour the Clegg Commission pay rises. Hugo Young, *One of Us: A Biography of Margaret Thatcher*, Final Edition (London: Macmillan, 1991), p.151; and Martin Holmes, *The First Thatcher Government 1979-83: Contemporary Conservatism and Economic Change* (Brighton: Wheatsheaf Books, 1985), p.107.

[3] Dunleavy, *Democracy, Bureaucracy and Public Choice*, pp.200-1.

[4] Dunleavy, *Democracy, Bureaucracy and Public Choice*, pp.204-5 and pp.239-48; also see Laurence E. Lynn, 'The Budget-Maximizing Bureaucrat: Is There a Case?' in Blais and Dion, eds., *The Budget-Maximizing Bureaucrat*, p.71; and Campbell and Naulls, 'The Limits of the Budget-Maximizing Theory,' p.89.

[5] J.C. March and J.P.Olsen, 'The New Institutionalism: Organizational Factors in Political Life,' *American Political Science Review*, Vol.78, September 1984, pp.734-5; Robert Grafstein, *Institutional Realism, Social and Political Constraints on Rational Actors*, (London: Yale University Press, 1992), p.12, p.82 and p.91; and John Campbell and Leon Lindberg, 'The Evolution of Governance Regimes,' in John Campbell, J. Rodgers Hollingsworth and Leon Lindberg, eds., *Governance of the American Economy* (Cambridge: Cambridge

from recent studies using a cross country comparison has highlighted the importance of institutional structure as the determinant of bureaucrats' behaviour and outcomes.[6] Though the motivations of actors are greatly influenced by the structures, institutions do not solely determine individuals' actions. An individual chooses to join an organization and whether to advance according to the established rules or work to change those rules.[7] Such findings highlight the need for a model to explain the differences between countries by incorporating institutional structures and a broader definition of bureaucrats' motivations.

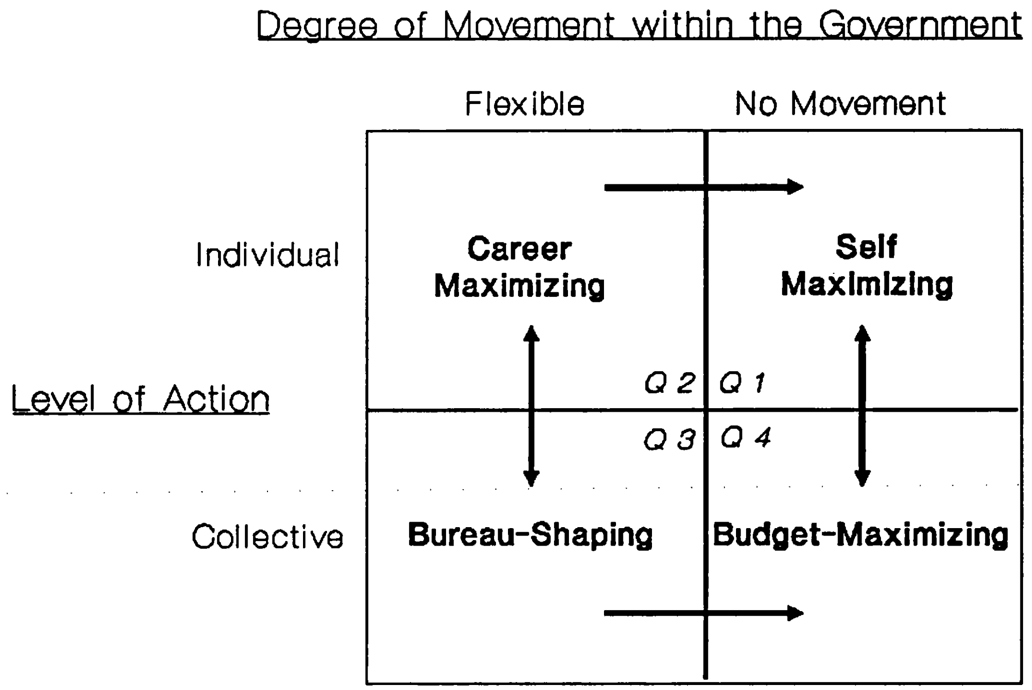
The remaining factor that needs to be addressed is why most scholars of bureaucratic behaviour have focused on the collective action of bureaucrats, and why very few examine individual strategies. Though Dunleavy correctly notes that a civil servant 'can most directly and strongly improve her personal position using an individual strategy,' he does not elaborate on what those individual strategies might be or when they will be used. In fact his bureau-shaping model itself only analyzes collective strategies. This ommision is especially surprising for public choice theorists because the individual as the basic unit of analysis in public choice theories. By focusing on collective strategies, we have been missing much of what is happening in government today.

University Press, 1991), p.327.

[6] Lynn, 'The Budget-Maximizing Bureaucrat,' pp.75-80; Campbell and Naulls, 'The Limits of the Budget-Maximizing Theory,' pp.99-104; Christopher Hood and Andrew Dunsire with Meg Huby, *Cutback Management in Public Bureaucracies: Popular Theories and Observed Outcomes in Whitehall*, (Cambridge: Cambridge University Press, 1989); and B.Guy Peters, 'The European Bureaucrat: The Applicability of *Bureaucracy and Representative Government* to Non-American Settings,' in Blais and Dion, eds., *The Budget-Maximizing Bureaucrat*, pp.306-7.

[7] David Silverman, *The Theory of Organizations: A Sociological Framework*, (London: Heinemann, 1972) Chapter 6 and pp.147-52.

Figure 6.1.: Strategies and Structures



The traditional view has been one of bureaucrats as budget maximizers, but budget-maximizing is only one of four possible strategies for bureaucrats (see Figure 6.1). To explain the different types of bureaucrats' behaviour, it is necessary to recognize the structures within which bureaucrats function and the means they have to maximize their utility. The most significant structural feature is whether the bureaucrat is tied to one bureau or department or whether there is movement between divisions and departments. The individual then has the choice of using individual or collective means to achieve his or her desired goals. As illustrated in Figure 6.1, in bureaucracies where there is little movement between departments, or such movement is only for demotion, bureaucrats will pursue strategies to enhance their immediate situation. As many studies have shown, this can be done in a collective manner by padding budgets, proposing large, inefficient projects and increasing the size of the department's staff, known as **budget-maximizing** (quadrant 4). But this can also be done on an individual level where civil servants will try to enhance their situation using numerous techniques ranging from delegating work to others to seeking additional job titles to hoarding departmental stationery; in other words, **self-maximizing** (quadrant 1). While the individual may chose between individual and collective strategies and many employ more than one strategy at a time (illustrated by the double arrows between quadrant 1 and 4), his or her situation is restricted by the bureaucratic structure.

Bureaucrats in a more flexible bureaucracy have less allegiance to one department and are therefore more concerned with their own personal advancement than with the growth or even continuation of their present department. This is done in a collective manner by contracting-out non-core functions and eliminating menial tasks, and is known as **bureau-shaping** (quadrant 3). It can also be done on an individual level. Techniques include working on high profile projects, efficiently implementing politically popular policies and protecting ones' superiors (on whom their promotions depend) or, in other words, **career-maximizing** (quadrant 2). Bureaucrats in more flexible bureaucracies can chose between individual career-maximizing and collective bureau-shaping strategies (as illustrated by the double arrows between quadrants 2 and 3). They also have more choices than their counterparts in restrictive bureaucracies because, in some cases, they can choose not to move between departments, depending on their own personal capabilities including limited managerial abilities. In these cases they can select self-maximizing strategies or if others have decided likewise, budget-maximizing strategies, (illustrated by the one-way arrows from quadrant 2 to 1 and quadrant 3 to 4).

Movement within bureaucracies can occur at three levels; between departments, between divisions within departments and within divisions. The greater the movement between departments, the more individuals will employ career-maximizing and bureau-shaping strategies. When movement is within divisions only, bureau and self-maximizing strategies are most likely. Movement between divisions but within a department presents an interesting intermediate case in which strategies are more likely to be mixed between career and self-maximizing, and between bureau-shaping and budget maximizing.

Next I examine why individual strategies will be most common in government bureaucracies. The difficulties of organizing collective action in general have been recognized by scholars at least since Mancur Olson's seminal work, *The Logic of Collective Action* published in 1965. To emphasize the difficulties of achieving collective action in governmental bureaucracies, I examine the conditions necessary for such actions (see Figure 6.2). Assuming that bureaucrats are rational utility maximizers, they will react to a policy change based on how they perceive the personal effect of the policy. What is personally negative is in part determined by the degree of movement in the bureaucracy or even within the department. When there is a high degree of movement, very few policies are actually perceived as personally negative because the civil servant can move to avoid such effects. Thus, most civil servants in flexible bureaucracies will not be threatened personally by change (Box 3 or 4 in Figure 6.2).

Bureaucrats' abilities to respond collectively are also determined by the strength of their department. A department's strength is a factor of its visibility,

Figure 6.2. Bureaucrats' Strategies:
Individual and Collective Responses to Policy Change

	Strong Department	Weak Department
Personally Negative Change	**Retaliate** collectively 2	1 **Resist** individually
Personally Positive Change	3 **Initiate** primarily individually but collectively possible	4 **Accept** individually

importance to the public, and political 'clout.'[8] Collective action will not be effective in weak departments and is therefore not worth pursuing. An individual in a weak department who perceives change to be negative will resist that change individually by employing a range of techniques from voicing concern to selectively revealing information to threatening to resign (box 1). An individual in a weak department who perceives change to be positive need not employ any strategy, just accept the proposal and work to implement it (box 4).

An individual in a strong department who perceives change to be positive may do the same as their counterpart in a weak department and accept it, or because of their greater resources may encourage the policy further by suggesting efficient ways

[8] Dunleavy, *Democracy, Bureaucracy and Public Choice*, p.181; and also from Hood and Dunsire, *Cutback Management in Public Bureaucracies*, p.49 - who have in turn extracted from Beck Jorgensen, 'The Management of Survival and Growth in Public Organizations,' paper presented at ECPR Joint Sessions, Barcelona, 1985.

to implement the policy or additional arguments in favour or even block alternatives (box 3). Should others perceive the same, these actions can be done collectively as well, though it will be less advantageous because credit for the success will be more difficult to attribute. A civil servant in a strong department who perceives change to be negative will fight back with all the resources available, including fellow colleagues and the department's assets. This might entail devising alternative strategies or embarrassing the ministers proposing the changes. Fighting back is of course a high risk strategy because failure may prevent further career advancement or reduce departmental functions, but because personal negative change may threaten one's job altogether, it may be worth the risk.

The evidence of this case supports these general assertions and provides additional examples of career-maximizing strategies. In this study, I focus on the top level civil servants (G1-7) in the Department of Energy and the Treasury. Higher level civil servants are the ones with the greatest ability to affect government policy. And while the Admiralty and later the Ministry of Defence, the Foreign Office, and the Department of Trade and Industry also had interests in the sales, they were less affected by them and therefore are only considered tangentially in this analysis.

6.1. Civil Servants as Career Maximizers

Contrary to conventional public choice models, privatization was not seen as a threat by DEn or Treasury employees, in part because it did not infringe on civil servants' jobs or the core function of the department. In fact, because privatization provided interesting work and a chance for some civil servants to be in the policy making limelight, it was generally well received.

Interesting Work and Career Advancement

The primary motivation for the civil servants I interviewed was interesting work. Drawing from their statements, but also their actions, career advancement was their primary objective. While interest in perks and lax work schedules would not be revealed to an outside interviewer, the frequency and variety of ways in which interest in their work was expressed suggests that it was a genuine factor, particularly since these opinions were often volunteered in the context of other questions. For example, one civil servant described the thrill of working on policies at the 'heart of affairs.' Another civil servant explained: The civil service is 'not badly paid, provides interesting work, is at the centre of power, and stimulating - especially times when working with ministers, but we're not power crazy.'[9] Civil servants' desire to be involved and even to influence policy in most cases could not be construed as wanting to initiate or independently make policy.[10]

Many of the civil servants recalled that their favourite periods in the civil service were when they were part of policy changes. The two periods most frequently cited by Department of Energy civil servants were the mid 1970s when the participation arrangements were being negotiated with the oil companies operating in the North Sea, and in the early 1980s when privatization was being implemented.[11]

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[9] Interviews with Department of Energy civil servants.

[10] Interviews with Department of Energy civil servants; reaffirmed by Wass, 'The Public Service in Modern Society,' p.11; and G.W. Jones, 'A Revolution in Whitehall,' *West European Politics*, Vol.12, No.3, July 1989, p.245.

[11] Based on interviews with 17 civil servants from the Department of Energy or the Treasury. This is confirmed by a recent study by Watson, 'Is Sir Humphrey Dead?' where she found, of the 28 civil servants she interviewed from across departments, 32% (the highest response) joined the civil service because the work would be interesting. This is also confirmed by Hugo Young's (*One of Us*) description of the welcome civil servants gave to Conservatives. He points to the fact that they were eager for firm policies.

Initially, DEn officials were unsure about oil privatization. As one civil servant described it, 'every conceivable shade of opinion was represented in the department.'[12] Over time the civil servants supported the sales because they provided interesting work, eliminated problematic responsibilities for the DEn and emphasized the importance of the Oil Division. One civil servant described being surprised at the time: 'Privatization, in fact, proved to be very interesting work.'[13] Another said working on a privatization bill was one of his 'happiest times' in the civil service.[14] The underlying importance of 'interesting work' was its connection to ministers and career advancement. Because a minister's recommendation could be crucial to a civil servant's promotion, officials were extremely sensitive to their ministers' goals and views. This is evident from the way DEn civil servants protected their ministers in Select Committee testimony, and also from the way they accepted their ministers' attitudes toward policies.[15] In part, work was interesting if it involved policies that their ministers advocated.

Summarizing the interviewees' responses, the reasons why privatization was interesting work can be grouped into four categories which also highlight the career-maximizing connection.

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[12] Interviews with Department of Energy civil servants.

[13] Interview with Department of Energy civil servant.

[14] Interview with Department of Energy civil servant.

[15] Testimony by Donald Maitland, House of Commons Energy Select Committee, 'Department of Energy's Estimates for 1981-82,' Second Report, *British Parliamentary Papers*, 1981-82, HC 231; House of Commons Energy Select Committee, Third Report, North Sea Oil Depletion Policy, *British Parliamentary Papers*, 1981-82, HC 337; House of Commons Energy Select Committee, First Report, BP/Britoil Job Losses and Asset Sales, *British Parliamentary Papers*, 1989-90, Vol.XX; and House of Commons Energy Select Committee, 'Wytch Farm (Disposal of BGC Assets) Memorandum by British Gas Corporation.'

(1) It was a newsworthy governmental policy. To be involved meant that the civil servants had the prestige of having their work discussed in the newspaper as well as among their clientele, the oil companies, and among friends and colleagues. Some of this status, though, may have come after the fact, which explains why the interviewees' memories were so positive.

(2) It was a new policy; the specifics were not predetermined. Civil servants therefore had room to offer suggestions and influence final outcomes. The DEn was the first government department to undertake large scale privatization, and hence was navigating uncharted waters. Civil servants described writing proposals and considering many different methods of sale, since the process was new and had not yet been worked out.[16] As one official explained, by 1980, there were

> several proposals under consideration for selling off, as well as other options and ways and means. We were writing one Cabinet paper a week. It was like the Labour party in '46 who came in to nationalize the coal industry; they got in and then didn't have a plan of how to do it. DEn began meeting with merchant bankers trying to work out how to do it.[17]

In these initial privatizations, the DEn took the lead, though many civil servants perceived privatization to be driven by the Treasury.[18] Civil servants found it stimulating to be involved in high profile policy projects, though it was more rewarding when proposals were accepted and they began to implement them under Lawson.[19]

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[16] Interviews with Department of Energy civil servants and minister; also see Lawson, *The View from No.11*, p.218.

[17] Interview with Department of Energy civil servant.

[18] Interviews with Department of Energy and Treasury civil servants.

[19] Interviews with Department of Energy civil servants.

(3) It was an achievable task with a clear end. So much of governmental work is on-going administration without clear goals or targets. Privatization provided a more satisfying sense of achievement. There was a clear end to a sale with large proceeds to show and work was created in the form of regulation of the North Sea. In the case of BGC's oil assets, civil servants had another result to show: Enterprise Oil. As one civil servant described it: '[We] made use of the situation and made another independent British company.'[20] Civil servant's attitudes toward the Wytch Farm sale emphasize how important the immediate result was. Because BGC was able to delay the sale for two years, instead of being exciting work and a specific achievement, they saw the sales as a long, drawn-out and frustrating process.[21] On the more humorous side, a civil servant pointed out the future tasks which the sales would create. He described civil servants before one privatization joking that they would be back in five years nationalizing what they were today privatizing.[22]

(4) It was a high profile policy. As such, work on privatization increased the civil servants contact with higher level ministers in their own department but also the Treasury. It also increased their contacts with outside experts, mostly from the City. For example, one civil servant noted the excitement of working with Nigel Lawson on the privatization legislation:

> When I was working on the privatization bill in 1982, Lawson would call me at home, rather than using his personal assistant to make the call. It was hard work, but these were some of my happiest times in the department. Lawson was stimulating to work for.[23]

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[20] Interview with Department of Energy civil servant.

[21] Interviews with Department of Energy civil servant and BGC executive.

[22] Interview with Department of Energy civil servant.

[23] Interview with Department of Energy civil servant.

Civil servants under Lawson were very careful with the handling of the policy. In fact, one civil servant who voiced some objections to policy change was told by other civil servants 'not to rock the boat.'[24] In theory, the development of privatization expertise would enhance a civil servant's future job prospects in the civil service as well as outside, though there is no evidence that any DEn civil servants were moved to oversee privatization in other departments nor any evidence of officials leaving to join merchant banks.

Further support for these four DEn civil servants' priorities is the way they were reflected in the civil servants' views of their different DEn ministers. One civil servant observed the general differences between the three ministers:

> Under Benn the department was in the wilderness. Under Howell, whose [political] stock was not very high, not much got done. Lawson was great; he would take decisions, and win.[25]

Benn lost his fight with the Cabinet over the retention of BP shares, as well as transferring ownership of the shares from the Treasury to the DEn. He was perceived by the civil servants to be outside the political mainstream both in British politics as a whole and within the Labour Cabinet where he consequently had little power. Civil servants complained that much of their time was spent implementing damage limitation measures. Benn was also notorious for being suspicious of civil servants, although this was not felt directly in the oil and gas divisions, and his stance caused a general tension in the department, which many civil servants saw as a reason for

[24] Interview with Department of Energy civil servant.

[25] Interview with Department of Energy civil servant.

low morale within the DEn at that time.[26] One BP executive even commented: 'I suspect that many of the civil servants were embarrassed by the things they were asked to do by Benn.'[27]

By contrast, David Howell was a much more middle of the road politician. Yet because of his personality and weak political links to the Prime Minister, many officials felt that things were no better under him. He did not accumulate much influence around Whitehall and rarely won his argument in Cabinet meetings. A few bitter civil servants complained that after losing in Cabinet, Howell would turn and blame them for his defeat. In general, while Howell was respected for his intellect, the consensus was that under him morale in the DEn was very low.[28]

Nigel Lawson was the DEn civil servants' preferred minister, but not because of his ideas (many admitted concern or alarm over some of his beliefs). Rather they were unanimous in praise of his leadership. Lawson was 'a breath of fresh air'. He was complimented for getting his way in Cabinet, for being decisive, and for being a team player. One civil servant described him as 'being demanding on those who worked for him, but that was okay when the department was winning,' and by another as 'the best Secretary of State I ever worked for.'[29]

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[26] Interviews with Department of Energy and Treasury civil servants and minister; Blackstone and Plowden, *Inside the Think Tank*, p. 81; and Geoffrey Fry, *The Changing Civil Service* (London: George Allen & Unwin, 1985), pp.15-7.

[27] Interview with BP executive.

[28] Interviews with Department of Energy civil servants and CPRS official; and Blackstone and Plowden, *Inside the Think Tank*, pp.82-3.

[29] Interviews with Department of Energy civil servants and CPRS official.

Not a Threat

At first glance, privatization appears to have caused, or at least coincided with, job losses in the DEn, as the number of jobs dropped from over 1,300 in 1976 to under 1,000 in 1991 (see Figure 6.3). While figures for the overall DEn are readily available, the break down by category is not as accessible. By combining the statistics published in a Select Committee on Energy report in 1981-82 with those published in the 1983-84 and 1986-87 Supply Estimates, it is clear that the number of civil servants working on oil matters decreased before privatization, but actually increased over the period in which the privatization occurred, 1982-87 (see Table 6.1). This is confirmed by informal estimates from DEn civil servants.[30]

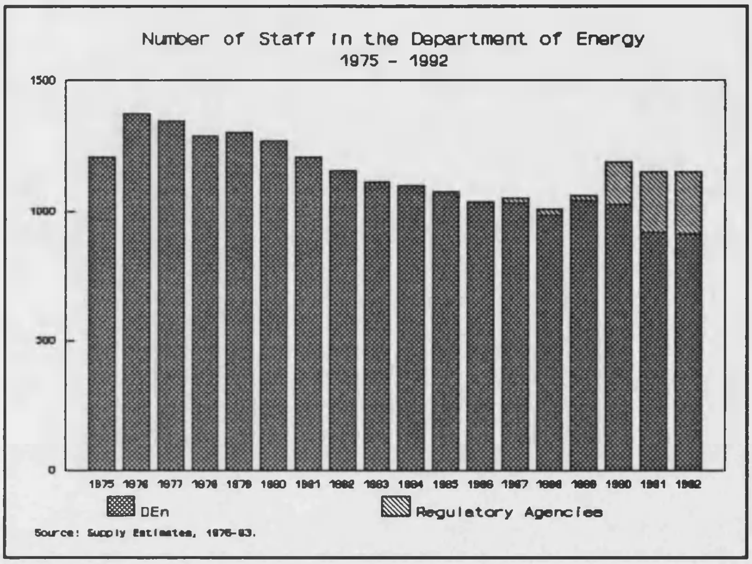

Figure 6.3.

[30] House of Commons Energy Select Committee, 'Department of Energy's Estimates for 1981-82,' Second Report, *British Parliamentary Papers*, 1981-82, HC 231; Supply Estimates for 1983-84, Class IV: Industry, Energy, Trade and Employment, *British Parliamentary Papers*, Vol.26, p.83; Supply Estimates for 1985-86, Class IV: Industry, Energy, Trade and Employment, *British Parliamentary Papers*, Vol.31, p.12; and interview with Department of Energy civil servant.

Table 6.1. Department of Energy Staff by Select Categories

	1979	1981	1983	1986
Employees in oil	390	337	334	359
Total DEn Staff	1267	1182	1135	1075
Percent of Total	31%	29%	29%	33%

Source: Supply Estimates, 1983-84 and 1986-87; and Select Committee on Energy, 1981-82, HC 231.

Because no independent regulatory agency was set up for the oil industry (as there had been for gas), the DEn itself was the only means left to regulate the oil industry. The DEn civil servants who I interviewed pointed out that new regulatory agencies that needed personnel were created in the wake of privatization, and that they had opportunities in other departments.[31] The second portion of the bar in Figure 6.3 represents the employees of the Office of Gas Supply starting in 1987 and the Office of Electricity Supply starting in 1989, which both employed many DEn civil servants. Also minimizing the harmful effects of the sales was the fact that though the DEn's overall staff numbers were decreasing during the early 1980s, overall salaries were increasing. Andrew Dunsire has calculated that while the number of total British civil servants declined by 14 per cent, salaries for those remaining increased by 21 per cent, though this did not compensate for the 52 per cent decrease

[31] Interviews with Department of Energy civil servants; also see Brian Hogwood and B.Guy Peters, *Policy Dynamics* (Brighton: Wheatsheaf Books, 1983), p.145; and Hood and Dunsire, *Cutback Management in Public Bureaucracies*, pp.123-4. But, as the government talks of privatizing internal functions, civil servants are expressing some concern for their future. See Peter Kemp, 'Mandarins are not the Only Fruit,' *Times*, 6 May 1993, p.18.

in salary which occurred during the 1976-80 period.[32] In the long run, however, all divisions of the DEn suffered job losses, and once the last shares of Britoil were sold, there were no more assets to sell nor the interesting work such sales provided.

A much greater threat than privatization came from the decline of North Sea oil production and DEn's amalgamation with the DTI in April 1993.[33] One civil servant estimated that by the end of 1993 the Energy Division was composed of only about 550 civil servants. In an effort to achieve economies of scale, the former DEn's central and economic forecasting services were combined with the DTI's .[34]

Generalism and Bureaucratic Behaviour

The generalist structure of the British bureaucracy helps to explain British civil servants' acceptance of privatization. The first point is that the civil service terms of employment provide greater job security than do contracts in the private sector. Thus, while a company selling off assets might find strong resistance from its employees, civil servants do not need to interpret policies in terms of the effect on their own future employment.[35] Change was an accepted part of being a civil servant. In this case, the most enthusiastic civil servants were young during the period, but there were others who were older and yet just as pleased to be part of something

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[32] Dunsire, 'Bureaucrats and Conservative Governments,' pp.192-4.

[33] Interviews with the Department of Energy civil servants.

[34] Interviews with Department of Energy civil servants.

[35] Adrian Ham, *Treasury Rules, Recurrent Themes in British Economic Policy* (London: Quartet Books, 1981), p.25. Although there is now talk of changing the career and therefore the job security aspect of the civil service, no measures have yet been implemented. See Fry, *The Changing Civil Service*, pp.150-3.

important.[36] One DEn civil servant stated emphatically: 'There were no old civil servants who opposed change. It was part of the nature of the job.'[37]

Three more factors specific to the British government accentuate civil servants' loyalty to implementing government policy rather than to defending their department or division. First, the British bureaucracy is a career civil service and senior officials are trained as generalists. They advance in many cases by moving between departments or at least undertaking 'tours of duty' in central departments. Consequently, the very strong organizational loyalties which exist in the United States government departments or in the British nationalized industries, for example, do not develop to the same degree.[38]

Cecil Parkinson described his frustration with the emphasis on promotion in the civil service:

> No Civil Service job ever seems to be an end in itself. It is all part of the process of training for the next job. I lost track of the number of times over the years that I discussed personnel changes with senior civil servants and heard the expression: 'This move will be very good for his or her career development.' Career development seems to be the number one priority, ranking way above actually doing any particular job. This means that however good the person is at the job he or she had, they will only be there for a matter of time before they are moved on to the next, and probably unrelated, job.[39]

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[36] Contrary to earlier finding by Ham, *Treasury Rules*, p.10.

[37] Interview with Department of Energy civil servant. However, in light of Mrs Thatcher's accusations about the civil service, officials were probably very sensitive to and defensive of questions regarding resistance to change.

[38] Hood and Dunsire, *Cutback Management in Public Bureaucracies*, p.35 and p.41; Campbell and Naulls, 'The Limits of the Budget-Maximizing Theory,' p.100; and Peters, 'The European Bureaucrat,' p.315. Only one of the Department of Energy civil servants I interviewed moved to private industry after serving in the department.

[39] Cecil Parkinson, *Right at the Centre: an Autobiography*, (London: Weidenfeld & Nicolson, 1992), p.153.

The second structural factor explaining civil servants' motivations was that promotions at the higher levels of the service are centralized. Rather than being reliant on the discretion of a bureau chief, civil servants depend for their advancement on their abilities as perceived by their professional peers, by ministers and (in very prominent cases) by the Prime Minister.[40] Criticisms were made that Margaret Thatcher in particular politicized the Permanent Secretary appointments. The (Conservative dominated) Treasury and Civil Service Committee, however, argued that there

> is no evidence that this is politicization in the overt sense of senior appointments being made on the basis of a civil servant's political affiliation. Instead, Mrs Thatcher has displayed a strong preference for what has been called the civil servant who embodies the 'can do' approach and is willing enthusiastically to implement the minister's policies.[41]

None of the civil servants I interviewed thought that political selection occurred even during the Thatcher era, with the possible exception of Peter Middleton's promotion

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[40] Hogwood and Peters, *Policy Dynamics*, pp.143-4; Lawson, *The View from No.11*, p.384; G.W.Jones, 'A Revolution in Whitehall,' pp.244-5; Drewry and Butcher, *The Civil Service Today*, p.169; F.F. Ridley, 'Career Service: A Comparative Perspective on Civil Service Promotion,' *Public Administration*, Vol.61, Summer 1983, p.198; and Hugo Young, *One of Us*, p.169 and p.337.

[41] Seventh Report from the Treasury and Civil Service Committee, 1985-86, Vol.I, para 5.9, as quoted in Drewry and Butcher, *The Civil Service Today*, pp.169-70. Ranelagh argues further that there is no evidence that Thatcher was promoting civil servants on a political rather than a merit basis. John Ranelagh, *Thatcher's People: An Insiders Account of the Politics, the Power and the Personalities* (London: Fontana, 1991), p.243. There is other evidence, however, that suggests senior promotions were politically driven. For example, Peter Hennessy (*Whitehall*) reports that the Labour government would not work with civil servants they saw as being politically promoted. And Denis Kavanagh suggests that a civil service is no longer above party affiliation with evidence of the increase in the leaking of secret documents to the press or to opposition MPs. Denis Kavanagh, *British Politics: Continuities and Change* Second Edition, (Oxford: Oxford University Press, 1990), p.253; also see Fry, *The Changing Civil Service*, p.27.

to Chief Secretary of the Treasury.[42] Yet they were well aware of the emphasis on action, and one civil servant described a shift in the civil service during the 1980s as one away from an emphasis on intellectual capability (i.e. political thinking) towards one on management capabilities.[43]

The third structural factor was that civil servants' responsibilities are so narrowly defined that they have few means to affect overall policy. Civil servants pointed out that their work was so focused that they would not have the time or the reason to know what their colleagues in other divisions, even in their own department, were pursuing. One said simply: 'I only know the people on this floor working in this area.'[44] More importantly, civil servants do not have any means of gaining the legislative authority necessary to create a policy. Civil servants cannot ask for Parliamentary time, submit a bill to Parliament or even participate, unless requested, in a Parliamentary debate.[45] However, civil servants do have a network of personal contacts in other departments gained by moving between ministries or by interacting on committees with officials holding related positions in other departments.

To assess the impact of these factors on career mobility, I traced what happened to the 73 senior DEn civil servants listed in the *Civil Service Yearbook* in 1982. By 1985, only 36 per cent remained in the same DEn division, a figure which was more than halved again to 13 per cent in 1988 and then fell to just 4 per cent by

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[42] Interviews with Department of Energy and Treasury civil servants.

[43] Interview with Department of Energy civil servant.

[44] Interviews with Department of Energy civil servants.

[45] Rose, *Understanding Big Government*, p.45; Campbell and Naulls, 'The Limits of the Budget-Maximizing Theory,' p.103; Fry (*The Changing Civil Service*) makes a more general argument that the influence of the civil service has often been overstated (pp.21-8).

1992. Over the time period of the major privatizations, 1982-88, less than one sixth of the higher level civil servants were in the same division in which they started while 40 per cent had left the department entirely (see Table 6.2).

Table 6.2. Percentage of Senior Department of Energy civil servants remaining in post or changing division or department, 1982 to 1988

	Total, N=73	
	1982-85	1982-88
Same division	36	13
New division	32	45
New department	10	15
Left civil service	22	26
Total:	100	100

Source: *Civil Service Handbook*, 1982, 1985, 1988 and 1992.

These statistics show that movement was in fact high within and out of the Department of Energy in the 1980s, supporting the connection between career-maximizing type strategies and a flexible bureaucratic structure. This connection is called into question by the fact that a quarter of officials who were in the DEn in 1982 subsequently left the civil service between 1982 and 1988. If they were forced to leave, this would negate the incentive for career-maximizing strategies. While reasons are not available for the DEn specifically, according to the *Civil Service Statistics*, during the 1980s at most 4% of all leavers were made redundant or retired pre-maturely 'in the public interest.' All others were voluntary resignations, retirements, deaths or illnesses.[46]

This movement is also supported by descriptive evidence, as a DEn civil servant related in terms of his department:

> In the Department of Energy there were mostly career civil servants in the administrative jobs. It was exceptional to be entirely in one department. Typically, civil servants moved to other departments. The brighter ones went to the Treasury for two or three years or stayed permanently, and a few came to the Department of Energy from the Treasury. Civil servants move more at the senior level, Permanent Secretary and Deputy Secretary, and at one stage there was an organized swapping program...Experience rather than expertise is the requirement. Civil servants are to know whom to ask, not necessarily know it themselves, like a barrister does. A few went to work for industry and one came back. When oil was found in North Sea, all engineers and geologists which made up the Petroleum Production Division came from private companies. Traditionally, civil servants have an Oxbridge background, more than half, but some have made their way up from the bottom.[47]

6.2. The Department of Energy: A Weak Department?

Drawing from the history of the Department of Energy (see discussion in Chapter Two) and accounts of civil servants, I estimate the relative strength of the Department of Energy over time (see Figure 6.4) using the four criteria mentioned above: size, visibility, importance and clout. Size is merely the measure of a department's staff and budget. Visibility is how much the public is aware of the department or the department's functions, which can be raised quickly though through specific events or crises. Importance measures the department's contribution to the country, either in terms of revenues or service. Clout is a measure of the department's connections and stature in Whitehall. This can be established over a long

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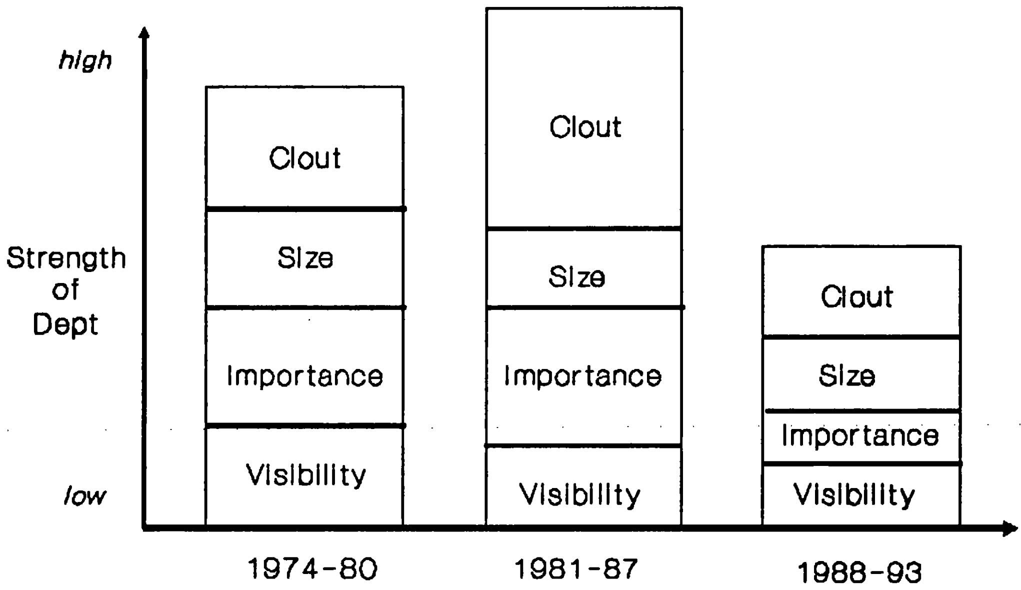
[46] HM Treasury, *Civil Service Statistics*, 1989-90, p.37.

[47] Interview with Department of Energy civil servant.

Figure 6.4. Strength of the Department of Energy 1974 to 1993: A Hypothesis



history or through the strong leadership of a minister.

During the initial period 1974-80, energy issues were very visible with the 1973-74 and 1979-80 energy crises; the department's role was therefore very public. Similarly, the department's importance in terms of influencing prices, ensuring supply and providing large revenues for the Treasury was also raised. Control of energy was also very important to Britain, and both of these were a large contribution to the department's strength. The department's size grew very quickly; having been formed in 1974 it reached its peak in terms of staff in 1976. The department's clout during this phase, however, was not high in Whitehall, with the exception of Lord Carrington (1974) and Harold Lever's (1975) brief service as the Conservative and Labour Secretaries of State respectively. Under Tony Benn and David Howell, for different reasons, the department suffered Cabinet defeats and endured poor leadership.

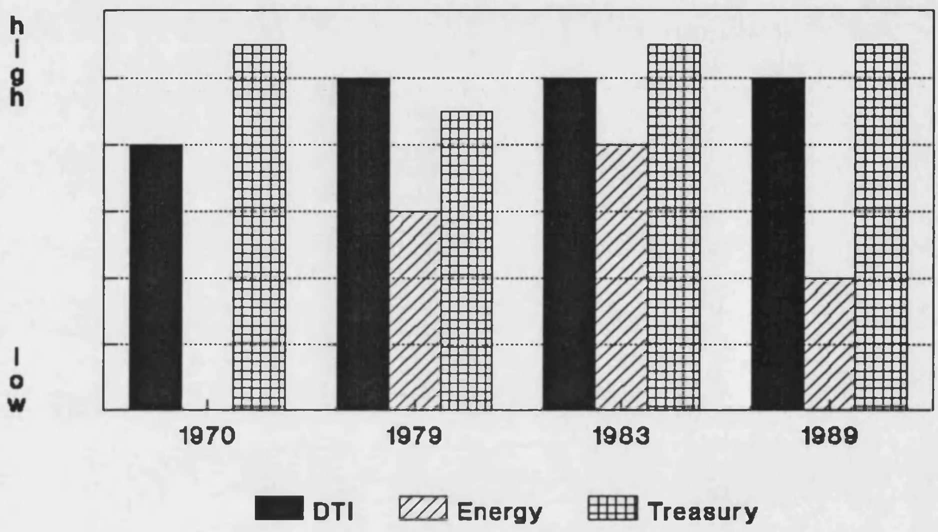
From 1981 to 1987, the department's strength reached its peak. While the department's visibility declined as energy supply issues subsided, this decline was partially compensated for by the visibility of the department's privatization programme and its new Secretary of State, Nigel Lawson. Similarly, compensating for the department's declining importance in terms of controlling energy supplies was the increasing importance of the department's privatization proceeds on top of its already large oil revenues. Oil revenues reached a peak in 1984 of £13 billion, enormous compared to the department's budget of £50 million.[48] In addition, privatization proceeds added £549 million to the Treasury's revenues in 1982, £617 million in 1984 and £450 million in 1985. The department's size had started to decline, though only slightly during this period. The issue that changed the most from the previous period, however, was that of the department's clout. As the leader in privatization and under the direction of Nigel Lawson, the department's clout in Whitehall was greatly expanded. Even when Lawson left in 1983 to become Chancellor, the privatization proceeds remained important to him and thus his contacts with the new Secretary of State and Cabinet veteran Peter Walker remained high.

After 1988, when the department's oil and gas assets had been sold, the more difficult sales of electricity and coal remained. In addition, with the drop in the price of oil, revenues from the North Sea also declined. As a result, the department's strength declined in terms of importance and size. In terms of visibility, DEn civil servants lamented, 'the lack of crises has lulled people into accepting the free market

[48] Supply Estimates 1983-84; and Central Statistics Office, *Financial Statistics*, May 1983 and May 1987.

and thinking that controls aren't necessary.'[49] In terms of size, the department's staff numbers and budget continued to fall. In fact, one of its Secretaries of State, Lord Wakeham had his job divided between Energy and special assignments for Thatcher.[50]

Figure 6.5. British Departments
Relative Strengths, 1970-89



The strength of a department is relative to other departments. Thus, in comparison with the Treasury and the Department of Industry (and later the DTI), the DEn was a relatively weak department in terms of budget and staff throughout, even

[49] Interviews with Department of Energy civil servants; and Blackstone and Plowden, *Inside the Think Tank*, p.80.

[50] Interview with Department of Energy civil servant.

at its peak in the 1981-87 period (see Figure 6.5).[51] Because civil servants perceived policy change in a positive way, they pursued career-maximizing strategies. A review of the civil servants' reaction to the oil asset sales provides further evidence.

Due to the semi-autonomous nature of the nationalized industries, DEn ministers were often embarrassed in the House of Commons because they could be questioned about all energy matters, including the activities of the nationalized industries over which the DEn had little control.[52] This proved to be a problem with BP, but more so with BNOC and BGC. In relation to BP, one DEn minister explained that 'the DEn has little say in the relationship.'[53] BP used its traditional links to the Treasury (which held the government's shares in BP) to secure influence with the government. Officials in the DEn found BP particularly difficult to deal with because the company was constantly trying to assert its independence. Many civil servants agreed that Shell was a more effective company in terms of supplying oil for Britain, and one civil servant argued: 'BP had not actually been a useful tool for energy policy matters'[54] Even so, the sale of the government's BP holding in 1977 and later sales were Treasury decisions.[55] Civil servants in the DEn were not consulted before the 1977 sale, although Tony Benn, as Secretary of State for Energy,

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[51] McInnes, 'Policy Networks,' p.22; Dunleavy, 'Architecture of the British Central State. Part II,' pp.412-3; and Christopher Hood and Andrew Dunsire with K.Suky Thomson, *Bureaumetrics: the Quantitative Comparison of British Central Government Agencies* (Farnborough, Hants: Gower, 1981), pp.143-4.

[52] G.W.Jones, 'A Revolution in Whitehall,' p.257; and interviews with Department of Energy civil servants and minister.

[53] Interview with Department of Energy minister.

[54] Interviews with Department of Energy civil servants.

[55] Interviews with Department of Energy civil servants.

was very vocal in his opposition. In 1979 the Treasury did ask the DEn whether the government's control of BP would be affected if their stake fell below the 51 per cent mark. Thus, the DEn's only contribution to the sales was the judgement that the government would maintain the same level of control with a sale.[56]

Though BP and the DEn worked closely together, and some argued that the department often favoured BP, this relationship could continue whether BP was government or privately owned. Because the closeness was often perceived negatively, some civil servants thought that private ownership would make it easier for the DEn to work with BP.[57] A BP executive emphasized the point:

> In the early days, BP did get an extra good cut. Civil servant Angus Beckett was fired for being too close to BP. That must be symptomatic of the fact that BP was too close. I rather doubted that he did favour BP too much. However, without his benevolence, the North Sea wouldn't have been produced as fast as it was.[58]

The reaction of DEn civil servants to BGC's asset sales provides an interesting illustration of civil servants' priorities. In its relationship with BGC, though the DEn often found that the corporation did things differently from the DEn's preferred course of action, they were proud of the corporation, and as a large company, it was one of their biggest clients.[59] Officials were frustrated, though, that their department could not stand up to the major nationalized companies it oversaw. Specifically, the DEn was unable to make BGC do anything it did not wish to do.[60] One DEn civil

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[56] Interviews with Department of Energy civil servants.

[57] Interviews with Department of Energy civil servants.

[58] Interview with BP executive.

[59] Interview with Department of Energy civil servant.

[60] McInnes, 'Policy Networks,' p.21; and interview with BGC executive.

servant described the nationalized industries boards as 'law unto themselves', and complained that board members and the chairmen were virtually impossible to unseat.[61] From the other side of the table, BGC executives argued that in the 1980s the 'Department of Energy understood what was going on, but it didn't account to a row of beans.'[62] The real aggravation was between BGC and DEn ministers because they were seen as impotent compared to Denis Rooke, the chairman of BGC. In the early 1980s, Rooke refused to even talk with ministers from the DEn.[63] The ministers made the argument that Rooke was getting too powerful and stood up to the government too much. Opinion among DEn civil servants, however, was mixed. For those working on the sale, the priorities were interesting work and high profile activities, not the long term viability of BGC. A civil servant not working on the sale, however, argued in favour of BGC, pointing out the competitive advantages for BGC to be in the oil industry.[64]

DEn officials' stances were more harsh regarding the Wytch Farm sale because of the embarrassing delays created by BGC managers' opposition. Because BGC administered the sale, the lengthy and frustrating progress emphasized the DEn's impotence which was publicly highlighted and keenly felt by DEn ministers and civil servants alike.[65] Many wished the government had waited until the 1982 Oil and Gas (Enterprise) Act which gave them clearer authority which they thought

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[61] Interview with Department of Energy civil servant.

[62] Interview with BGC executive.

[63] Interview with Treasury civil servant.

[64] Interviews with Department of Energy civil servants.

[65] Interview with Department of Energy civil servant.

would have strengthened their position vis a vis BGC and facilitated the sale. The sale of Enterprise Oil provided some spiteful pleasure for DEn ministers, but was viewed merely as a more successful implementation of policy by civil servants, who this time had complete control of the transaction. As one BGC executive explained, they 'just told us what to do.'[66]

From the DEn's perspective as a whole, or the Oil Division in particular, there were no strong reasons to keep BNOC or Britoil. A civil servant explained that DEn relied more on licensing awards than it did on BNOC to influence events in the North Sea.[67] On the one hand, the sale of BNOC imposed no negative effects because it did not reduce the DEn's capabilities. On the other hand it provided two positive effects: It reduced the tension between the companies and the DEn, and the creation of Britoil fulfilled a DEn objective of encouraging regular British commercial involvement in developing the North Sea.

The 'friendly tension' between the DEn and BNOC began when the company was created. The department's officials were jealous of BNOC in the 1970s because the BNOC staff got better terms and working conditions than DEn's civil servants.[68] The agencies were thrust together immediately to negotiate the North Sea oil participation agreements, which is how some of the animosity began. As one DEn civil servant admitted, BNOC executives had a brasher but a more effective style. The DEn was concerned that in carrying out a role for itself, BNOC was destroying

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[66] Interviews with BGC executive and Department of Energy civil servant.

[67] Interview with Department of Energy civil servant.

[68] Interviews with Department of Energy civil servants.

the government's long term relationships with the private oil companies.[69] On a professional level, BNOC had better technical skills and more direct access to information. In addition, BNOC was given the statutory duty to offer advice to the government, and DEn civil servants were irritated by the fact that the company took full advantage of this formal power.[70] However, there were also some strong ties between the DEn and BNOC. The DEn appointed two civil servants to the board of BNOC, and a few civil servants were also seconded to the company. Both steps eased communication problems and helped relations. The civil servants who worked with BNOC were proud of the company's accomplishments.[71] Most civil servants, however, recognized that a constant level of tension was sustained merely by BNOC doing things differently from the way DEn wanted them. Rather than being antagonistic or offensive, one civil servant explained, BNOC was merely 'inconvenient'.[72]

One of the most striking features of my interviews with BNOC executives was their enthusiasm for ensuring British development and control of North Sea oil. This was markedly different from the more politically pragmatic view of DEn civil servants. The result was that some DEn officials felt that BNOC was at times 'unnecessarily extreme.'[73] The DEn civil servants' saw BNOC's enthusiasm for getting more than the required percentage of oil refined in the UK - surpassing the

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[69] Interviews with Department of Energy civil servants.

[70] Interviews with Department of Energy civil servants and minister.

[71] Interviews with Department of Energy civil servants.

[72] Interviews with Department of Energy civil servants.

[73] Interviews with Department of Energy civil servant and minister.

DEn's requirement - as naivety (see Chapter Five). As one civil servant explained: 'The more you know about refining in the UK, the less feasible [the policy] was.'[74] Another civil servant pointed out that the DEn had other constraints which BNOC did not have, including the EC, the Treasury's budget pressures and the interests of the private sector.[75] The DEn saw the policy as a politically necessary target that need not be adhered to in practice, so that whenever a waiver was requested by an oil company, it was granted. Some DEn civil servants also feared that BNOC was or would become too powerful.[76] This was felt even more strongly by the ministers: 'BNOC was becoming so damn powerful,' and there was already the precedent that 'Statoil was practically dictating to the Norwegian government, and that BGC and the NCB were already enormously more powerful than the government.'[77]

Some of the differences between the DEn and BNOC can be explained by their different goals and constituencies. The DEn's main client in terms of oil and gas policy were the private oil companies and their promotion depended on ministers. BNOC, in contrast, competed with the private oil companies - and had a notoriously antagonistic relationship with them, and their jobs were relatively secure from ministerial intervention.[78] As one civil servant saw it, BNOC wanted to make decisions about the North Sea and emphatically did not want the private sector oil companies to be making such decisions. The big oil companies, however, wanted

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[74] Interviews with Department of Energy civil servants.

[75] Interviews with Department of Energy civil servants.

[76] Interview with Department of Energy civil servant.

[77] Interview with Department of Energy minister.

[78] Interview with BNOC executive.

freedom to operate, and applied pressure on the DEn to achieve this goal.[79] One civil servant described the DEn as playing 'the role of honest broker between the companies and BNOC.' However, a BNOC executive found that if 'the industry was lobbying the department on a particular point, it would take a very strong argument for the department to back BNOC.'[80]

The one example where the department's core functions, and as such, civil servants' immediate work tasks were threatened was in 1983 when the Treasury sought to end the department's discretionary licensing system in favour of auctions for licences. Though this had been tried in 1971, it had not resurfaced until 1983 when ironically the DEn was at the zenith of its power. Being at its strongest, we could expect collective action with a chance of success. Though auctions actually took place in the 1983 licensing round, they were only for seven blocks while the other eight blocks were awarded according to the department's discretionary criteria. This appears to be a one-off foray as the auctions were not repeated subsequently. The strategies employed to secure that the auctions were not repeated included emphasizing that the discretionary nature of the licences enabled the DEn to ensure: (1) acceptance of the terms of royalties, (2) government had current information about the North Sea, including potential tax revenue, (3) profits of foreign companies were not repatriated, (4) the oil companies purchased British supplies, and (5) British companies were awarded a reasonable share of the North Sea.[81] Thus, the

[79] Interview with Department of Energy civil servant.

[80] Interviews with BNOC executive and Department of Energy civil servant.

[81] Interviews with Department of Energy civil servants.

department also had important political allies in the British oil companies.[82] How these arguments were made, individually or collectively, by DEn officials or the British oil companies was not revealed through my interviews. The first time the auction option was suspended was after the 1971 auctions, before the Department of Energy was even created. But because the licences were issued by the strong DTI, it is not surprising that the civil servants were able to fend off future auctions. It is surprising though that the second challenge came at the height of the DEn's power, and as such accentuated the DEn's relatively weak position versus the Treasury.

6.3. The Treasury's Threat

As the department in charge of all spending, the Treasury was an interested player in the activities of the nationalized industries, including BP, BNOC and BGC. In addition, as a 'super-control' agency which oversaw the central government organization as a whole, the Treasury had the means to influence the future of the companies.[83] Its encouragement of the DEn's privatizations can be seen as a collective-action strategy to ward off threats to its own core functions.

While the Treasury had the reputation of being the most powerful department staffed with the best and brightest civil servants, it attracted some criticism early on

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[82] Interviews with Department of Energy civil servants.

[83] Pliatsky, *The Treasury Under Mrs. Thatcher*, p.3; Blackstone and Plowden, *Inside the Think Tank*, p.83; Richard Rose, 'British Government: The Job at the Top,' in Richard Rose and Ezra N. Suleiman, eds., *Presidents and Prime Ministers* (Washington, DC: American Enterprise Institute for Public Policy Research, 1980), p.39; and Dunleavy, 'The Architecture of the British Central State, Part II,' p.400. Keith Middlemas (*Power, Competition and the State)*, however, questions this preeminent role, arguing that some of the biggest adjustments made post World War II in foreign affairs and defense took place without Treasury review (p.456).

in the Thatcher government.[84] Thatcher and her Cabinet colleagues questioned the Treasury's capabilities, especially with regard to the PSBR, an innovation of the Treasury's in the 1960s. As the residual between two very large numbers, the government's income and expenditure, the average error in the PSBR over the decade of the 1970s in fact was about £3 billion - 1.5 percent of GDP; these errors continued into the 1980s.[85] Not trusting the Treasury civil servants, Prime Minister Thatcher and Chancellor Howe both appointed outside advisers to brief them and proceeded by assuming that the Treasury could not be trusted to deal with public spending alone.[86] The Treasury's defense was that the PSBR was the difference between two huge numbers which were not easy to predict. Beginning with the IMF crisis in 1976, Treasury civil servants came out against policy being strongly focused on the PSBR because it was so variable.[87] But Treasury officials of course thoroughly agreed with the Conservatives on the desirability of controlling public expenditure.[88]

The Treasury had means to alter the PSBR figures in the short-term. A former

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[84] Pliatsky, *The Treasury Under Mrs. Thatcher*, p.13; Anthony King, 'Margaret Thatcher: The Style of a Prime Minister,' in Anthony King, ed., *The British Prime Minister*, Second Edition, (London: Macmillan, 1985), pp.48-9; Jim Prior, *A Balance of Power*, (London: Hamish Hamilton, 1986), p.122; and Lawson, *The View from No.11*, p.26.

[85] Walters, *Britain's Economic Renaissance*, p.80; and C.N. Morris, 'Budgetary Arithmetic and the 1982 Budget,' in John Kay, ed., *The 1982 Budget*, (Oxford: Basil Blackwell, 1982), p.94.

[86] Hugo Young, *One of Us*, pp.152-3; Thatcher, *The Downing Street Years*, p.134; Judy Hillman and Peter Clarke, *Geoffrey Howe: A Quiet Revolutionary* (London: Weidenfeld & Nicolson, 1988), pp.143-4; William Keegan, *Mrs. Thatcher's Experiment* (London: Penguin Books, 1984), p.167; also see Middlemas, *Power, Competition and the State*, p.237, p.246 and pp.275-6; Lawson, *The View from No.11*, pp.960-1; and Ranelagh, *Thatcher's People*, pp.228-30. The idea of a 'counterweight to the Treasury' was not new, see Hood and Dunsire, *Bureaumetrics*, pp.168-9.

[87] Interview with Treasury civil servant.

[88] Hugo Young, *One of Us*, p.155.

Chief Secretary of the Treasury, Joel Barnett, recalled that 'finding ways of cutting the PSBR without having any real effect, especially on employment, occupied our most fertile minds' - an activity which he refers to as 'fiddling the figures'.[89] One former Treasury adviser recalled that during his time at the Treasury, he could change the PSBR by £1 billion in the course of a morning's work.[90] However, these illusions could not be sustained indefinitely.

Privatization as a negative contribution to spending was useful to the Treasury. According to a former official, privatization

> has gone farther and faster than was ever planned at the outset, and the receipts from these special sales of assets have helped significantly in reducing the need for public borrowing.[91]

Under pressure to get the numbers right, the Treasury became more vigilant against arrangements that would delegate spending power. They also became more interested in short-term cost control measures, even at the expense of longer term benefits.[92] Privatization became one of those short term measures.[93] The fact that proceeds from privatization were counted as negative spending was one of the most important factors in the decision to sell BP shares in 1977. As one politician explained, in terms of its effect on the balance sheet, 'selling shares had the same effect [on the PSBR]

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[89] Gardner, *Decade of Discontent*, p.120.

[90] Donald MacDougall, Economic Adviser to the CBI and a former Treasury adviser, quoted in Prior, *A Balance of Power*, p.131.

[91] Peter Riddell, *The Thatcher Decade: How Britain Has Changed During the 1980s* (Oxford: Basil Blackwell, 1989), p.91; and Pliatsky, *The Treasury Under Mrs. Thatcher*, p.24 and p.112.

[92] G.W.Jones, 'A Revolution in Whitehall,' p.257.

[93] M.R. Garner, 'British Airways and British Aerospace: Limbo for Two Enterprises,' *Public Administration*, Vol. 58, Spring 1980. Garner was formerly an Under-Secretary in the DTI; also see 'Government to Retain 49% of State Oil Assets,' *Times*, 21 October 1981, p.1.

as cutting old age pensions...the government always cut where it was easiest.'[94] Had share sales been counted as revenue, the government's spending totals would have been higher, revealing how difficult it was for the Treasury to actually decrease spending.[95]

The costs to this strategy were minimal in the short term because, as with the DEn, the government's companies with oil assets caused the Treasury problems and did not provide obvious benefits. The Treasury and BP were on fairly good terms with each other; they shared the common goal of increased profits, and met on an annual basis to discuss BP's dividends. While BP saw the Treasury as an ally, not everyone in the Treasury was a enthusiast of BP. In fact one of the civil servants involved with BP, like some officials in the DEn, thought that the company provided no advantage to Britain, and that Shell did more to serve the country.[96] Most civil servants in the Treasury were in accord with BP in wanting the complete sale of the government's shareholding.[97]

The Treasury had the most difficulty controlling BGC's finances. As BGC's financial arrangements were made in the 1972 Gas Act, when the company was loss making, they focused primarily on loan arrangements and did not specify how profits would be allocated (see discussion in Chapter Five). Because of this, BGC later retained most of its earnings.[98] The Treasury thus sought means to break BGC's

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[94] Interview with Treasury minister.

[95] Pliatsky, *The Treasury Under Mrs. Thatcher*, p.36.

[96] Interviews with Treasury civil servant and BP executive.

[97] Interview with Treasury civil servant.

[98] Interview with BGC executive.

control, first by creating a new gas tax in 1981, and later by forcing the sale of BGC's oil assets, Enterprise Oil and Wytch Farm. As one official explained: 'The Treasury felt that the sale could help the PSBR. But the issue really was one of rationalizing the interests of BGC.'[99] The government felt that a national gas company should not be involved in oil too.

Turning to BNOC, the Treasury was sceptical about the enterprise from the beginning. As one Treasury civil servant explained, BNOC was

> an unnecessary brass plate company. The government already had the power it needed to control the North Sea. BNOC just oversaw paper transactions of the sale of oil; they had no relevance. They had little or no management, with their equity stakes they were just sleeping partners... the government had the power it needed to control the North Sea, such as taxes and regulations.[100]

The Treasury also had problems controlling BNOC's expenditure, despite the control measures written into the company's charter. The Treasury's orientation towards saving money often put Treasury officials at odds with BNOC, whose goal was the expansion of its oil business. Particularly when BNOC was being created in the mid-1970s, these spending constraints limited what the company could do.[101] However, as BNOC grew with the acquisition of Burmah Oil's assets and was able to raise funds in the private market, the Treasury mattered less to its development.

Eventually, BNOC was able to thwart the Treasury's controls. Working in the private sector, BNOC had to abide by private sector business practices. The North Sea oil fields were operated through consortia of companies and run by the partner

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[99] Interviews with Treasury civil servants.

[100] Interview with Treasury civil servant.

[101] Interview with BNOC executive.

with the majority holding, and all partners were bound by law to contribute according to the schedule agreed with the majority partner. Therefore, when BNOC had a minority holding, investment schedules were determined by the stronger partners and the Treasury's hands were tied. As a BNOC executive pointed out: 'if BNOC was seen to be constrained by the government, then BNOC would find it very hard to join consortiums for licensing rounds.' He concluded that 'while the Treasury had control in theory, in practice it didn't really.'[102]

There is one exception where the Treasury was able to defer development of BNOC's interests. Because BNOC was the majority partner in the Clyde field, BNOC and, *de facto* the Treasury, could control the development schedule. In the name of a graduated depletion policy, the government delayed the development of the field for five years. It was well known, however, that the Treasury was opposed to any restrictions on production and the ensuing taxes, so many saw the delay as the lack of funds because of pressure on the PSBR. BNOC executives argued fiercely with the Treasury that their reputation as an operator of profit-making fields would be ruined and in the end compromised with a three year deferment of the development of the field which was long enough for Britoil to be privatized and the investment burden to be transferred to the private sector.[103]

Even though BNOC's expenses were reported outside the PSBR, the Treasury was tied to ventures in an inherently risky business. To stem BNOC's expansion, the Treasury supported the move to sell BNOC's exploration acreage. They were also placated against any more intrusive moves in the first round of spending cuts by the

[102] Interviews with BNOC executives.

[103] Interviews with Department of Energy civil servant and minister and BNOC executive.

forward sale of oil.[104] The Treasury was aided by the Conservatives' support and BNOC's assistance with measures that avoided privatization. One of the proposals made by BNOC in 1980 to prevent the privatization of its production operations was to sell bonds to the public. The Treasury opposed this proposal because they feared all future profits would accrue to the bondholders rather than to the Treasury, while the proceeds from the bond offerings would yield less than a straight-forward sale of the production assets.[105]

The reason for the Treasury's reserve over BNOC, Sir Alistar Morton complained, was because they did not understand the oil business:

> In February 1980, civil servants came to me to ask how much the company was going to borrow or retain by the end of March because the PSBR was really tight. I asked them how much they wanted the amount to be. They said that this was a serious meeting so asked again how much money do you want, and I explained I had 10 or so tankers at sea for which I could pay or get paid before or after March. When I told them I had £50 to £70 million to swing either side of March, the civil servants were amazed, as they were only looking for £1 million or so. They just didn't understand the magnitude and power of oil.[106]

One final point of contention was also resolved when BNOC was abolished. BNOC set the price for oil and the Treasury's revenues were dependent upon that price. A higher price meant higher Treasury revenue, yet this was often in conflict with BNOC's own goals, such as increasing the amount of oil refined in the UK, and profits, especially when the price of oil was falling.[107] The conflict was resolved once BNOC was abolished because the Treasury took over the role of deciding the

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[104] Interviews with Department of Energy civil servants and minister.

[105] Interview with Department of Energy civil servant.

[106] Interview with Sir Alistair Morton, 15 October 1993.

[107] Interview with Treasury and Department of Energy civil servant and BNOC executive.

tax reference price.[108]

From 1983 onwards, with the level of the PSBR improving, the Treasury's policy-making role expanded again. In part, this was due to the proceeds from the oil asset sales. One sign of the Treasury's rehabilitation was that Prime Minister Thatcher appointed the Treasury the lead department in charge of co-ordinating the whole privatization programme. Because it increased their control over spending and receipts, the Treasury was one of the few parts of Whitehall to be fully committed to the new strategy, and the only department in the central position necessary to make the concept into a coherent policy and the central theme of the Conservatives' second term in government.[109] Symbolizing the Treasury's strength compared to the DEn, no DEn civil servants were moved to the Treasury, even though the DEn was the department with the most experience with privatization.[110]

In terms of department strength and collective action, unlike other measures, encouragement of the privatization programme could not be done at the individual level. The coordination, planning and perseverance by Treasury officials demanded collective action for success. Ironically, the strategy was to shape another department rather than their own, which emphasizes the point that different options are available to departments with different levels of strength. As possibly the strongest department in Whitehall, 'government-shaping' may be a strategy uniquely available to the Treasury.

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[108] 'Free at Last,' *Economist*, 16 March 1985, p.77.

[109] Lawson, *The View from No.11*, p.7; Abromeit, 'British Privatization Policy,' pp.74-5; and Riddell, *The Thatcher Decade*, p.92.

[110] Interview with Department of Energy civil servant.

Conclusion

The traditional public choice view is that bureaucrats are budget-maximizers, but based on a structure and means typology, I argue it is only one of four possibilities. As such, bureaucrats can also be bureau-shapers, self-maximizing and career-maximizers. Because British civil servants have a high degree of mobility within the government bureaucracy, their loyalty is to the central government apparatus as a whole rather than a particular department or division. As such, few policies are perceived as personally negative, so that rather than fearing for their own survival, their primary interest is in work tasks. An important element of that definition is as its use as a vehicle for promotion, apparent from officials' emphasis on contact with ministers and top level civil servants, and definable projects where success can be easily determined. Part of this analysis is drawn from civil servants' direct statements, which contradict broader surveys on the subject of civil servants' priorities, but this is not surprising as career advancement is not necessarily the kind of goal a civil servant wants to reveal. Support for this analysis is also drawn indirectly from the civil servants' descriptions of their ministers which fit well with previous research on ministers.[111]

Though the strength of the DE rose and then declined again, it was relatively weak compared to the Treasury and DTI throughout, and it is therefore not surprising that no collective strategies were detected in the DEn. The individual strategies observed, adding to our definition of career-maximization, included: providing feasible means of implementation, preventing other civil servants from objecting,

[111] Simon James, *British Cabinet Government* ((London: Routledge, 1992), pp.36-7; Hogwood and Peters, *Policy Dynamics*, p.139; and Sue Cameron, 'Fortune Come Up Trumps,' *Times*, 27 June 1987.

working the long hours necessary, and facilitating ministers' wishes. The Treasury, however, as a strong department with its core functions under threat did employ collective strategies to regain it pre-eminence over PSBR planning. One of the strategies included encouraging privatization in other departments, suggesting that as a super-strong department, the Treasury may have a unique option available to it - government shaping.

Turning to a larger debate on the subject, there is some fear that the generalist structure which provides room for political influence on civil servants' careers has politicized the British civil service unduly. This generalist structure, however, is the key factor in this study that enabled officials to be cooperative with privatization policy. Rather than party loyalty, British civil servants are committed to the existing government. As such, when officials are presented with new policies by new political masters will implement the policies cooperatively as they did their antipodes. The real problem is not politicization, but rather short-termism. Civil servants implement policies and then move to another department. They therefore have little accountability for their work in the long-run. The elimination of the flexible structure would increase long-term accountability, which combined with politicians' notorious short-terms horizons might provide a useful balance. This structure also encourages self and budget-maximization, and would increase the civil servants' reputation as the politicians' nemesis.

Chapter Seven: Politics, Careers and Elections

Most theorists who explain privatization focus on the later stages of the Conservatives' programme,[1] yet these later stages differ markedly from the development stage of the policy. Originally it was a short-term programme, to address pragmatic fiscal considerations. It grew more radical over time.[2] Most theories of privatization cannot explain why politicians selected a policy in the face of little policy demand and proceeded in an ad hoc manner.

Existing public choice theories of policy-making focus primarily on the demand for policies, such as the traditional 'median voter' model which assumes that a politician's primary goal is to be (re) elected and predicts that to do so a politician will select policy positions to appeal to the largest number of voters.[3] The model cannot explain, except because of a lack of information, why politicians would choose a policy position which favours only a minority as was the case with privatization in Britain, especially of the oil assets. While public opinion did begin to shift towards private ownership in the 1980s, the majority was always opposed. A more accurate measure of demand, I suggest, includes the level of intensity of opinion for that policy because only when intensity is high will citizens cast a vote accordingly. As I show in this chapter, the majority of opinion on privatization was weakly felt and

[1] Marsh spends four paragraphs on the Conservative's first term (p.460-1) while the remainder of the article focuses on the aims and achievements of their second term. David Marsh, 'Privatisation Under Mrs. Thatcher: A Review of the Literature,' *Public Administration*, Vol.69, Winter 1991.

[2] Abromeit, 'British Privatization Policy,' p.83.

[3] Mueller, *Public Choice II*, pp.180-2.

thus, most votes were cast according to opinions on other issues. Other factors must therefore be at work in order to explain why the Conservatives raised privatization on the policy agenda and selected the policy position they did. There are, however, few supply-side explanations of policy-making which might explain the Conservatives' choices.

Since public demand does not readily explain the privatization stance, elite theory is often proposed as an alternative. Elite theorists argue that 'elites have introduced the policy [of privatization] because of a belief that this would be technically more efficient, as well as consistent with the ideological principles of rightwing parties or 'post socialist' parties of the left.'[4] If elites were the driving force, we would expect a coherent programme using a logical progression to move state-owned businesses into the private sector. Instead, the early privatizations were done in an ad hoc manner with an emphasis on Treasury revenues over efficiency, and the sales were primarily of companies already operating in the private sector.[5] In the case of the oil sales, for example, ownership made no difference to the operations of the company. In addition, the theory fails to explain why elites came to believe in privatization in the late 1970s and early 1980s rather than another point in time, or why they nationalized the companies in the first place.

There are few other supply-side explanations. Public choice theorists' attention to the supply-side of policy-making has been limited to logrolling by special interest

[4] McAllister and Studlar, 'Popular Versus Elite Views of Privatization,' p.158; also see Wolfe, 'State Power and Ideology in Britain.'

[5] Abromeit, 'British Privatization Policy,' p.83.

groups, pork barrel politics and capture of agencies by external interests.[6] In terms of elections and policy position, public choice theorists focus on preference-shaping activities where politicians seek either to foresee public demand and plan accordingly or act to alter structural factors so demand will alter to suit their policies.[7] Dobek adopts this view in explaining privatization in Britain, arguing that Tory politicians sought to expand the number of Conservative voters through wider-share ownership. Dobek emphasizes that the key was the politicians' perception of the policy's effect, not necessarily the actual outcome. Dobek's explanation, however, is not supported by the politicians' actions on the oil asset sales. These sales were distinctly ad hoc, beginning with the Labour government in 1977 and were not timed for elections or other publicity. In addition, none of the oil sales targeted new shareholders. In fact, the government purposely did not advertise or encourage wider share ownership because oil was an inherently risky business.[8]

A better supply-side explanation is therefore necessary to explain why both the Labour and Conservative governments chose to sell oil assets to existing shareholders with minimal publicity over a ten year period with, at best, weak public demand for the sales. I suggest that the policy choice can be described as a multi-step decision tree (see Figure 7.1). The first branch stems from the demand for the policy. If there is large demand, politicians have very little room for choice and, therefore, adopt the policy where the demand and intensity are highest as more traditional theories predict.

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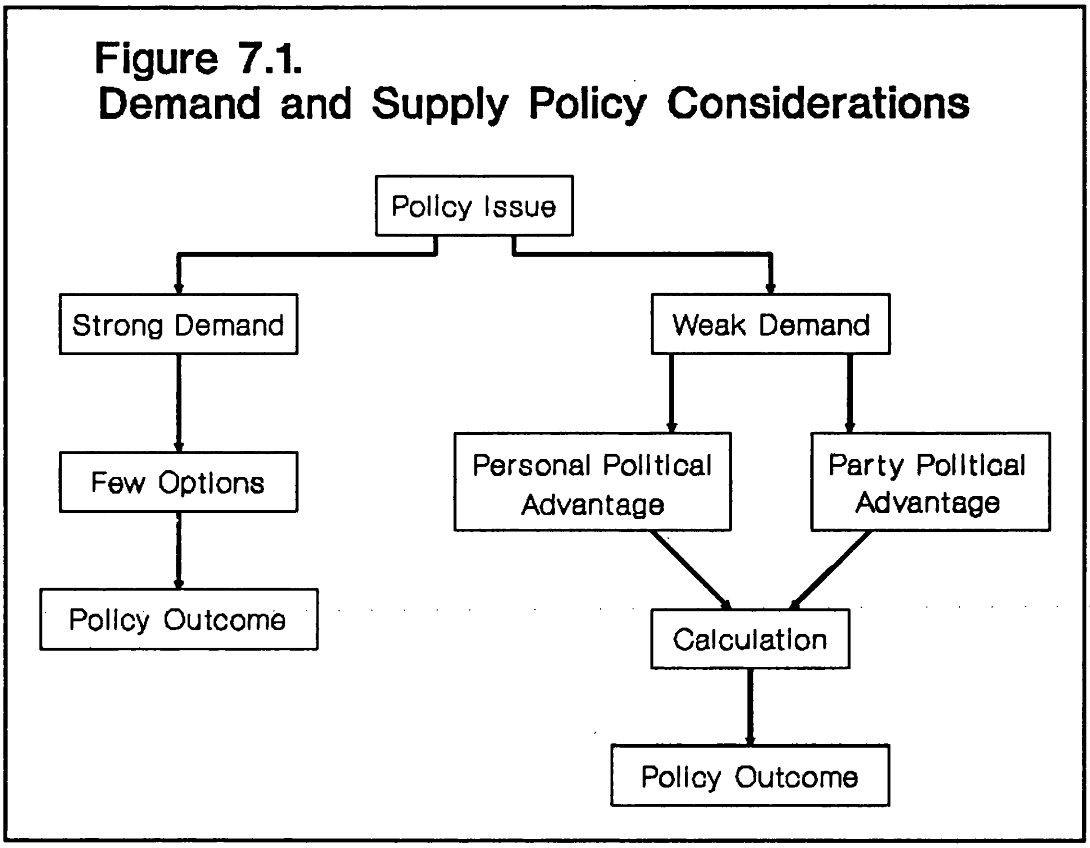
[6] Patrick Dunleavy and Brendan O'Leary, *Theories of the State: The Politics of Liberal Democracy* (London: Macmillan Education, 1987), p.112.

[7] Dunleavy, *Democracy, Bureaucracy and Public Choice*, Chapter 5.

[8] Britoil, 'Offer for Sale'; and Enterprise Oil, 'Offer for Sale.'



When there is low demand (not opposition), the process is very different because politicians have greater discretion in whether to select a policy and how to implement it. Politicians then calculate according to two different sets of criteria, personally and electorally. (1) The personal calculation is whether the policy will provide individual political advantages to politicians such as a promotion into the Cabinet or an increase in their public profile. (2) The party political factors are a complex calculation comprising two additional sets of factors: the concentration of costs and benefits to supporters and opponents over time, and the position and intensity party members. Depending on the combination of these factors, the policy is rejected or it is adopted and the most advantageous position selected, which was the process in this case.

Both personal and party supply factors are necessary for the adoption of a policy. To be adopted, a policy must have an entrepreneur willing to bear the initial costs of developing the policy. To entice a politician to take on such costs, there must be clear personal advantage to be gained. In addition, there must be clear electoral advantage for the party to adopt the policy and risk tainting all their candidates with an unpopular or infeasible policy. The necessary combination of these personal and party political factors is represented in Table 7.1. To be selected, either personal or party political advantage must be strong (+) to provide the impetus. Selection will be facilitated if both are strong, however, as long as neither are opposed (-), i.e. their stance is positive or neutral (0), policy selection is possible. Opposition from either factor is normally too large of an obstacle to overcome, especially as other policies may offer easier alternatives.

Table 7.1.
Combinations of Personal and Party Political Factors

		Party Political Factors		
		(+)	(0)	(-)
Personal Political Factors	(+)	Yes	Yes	X
	(0)	Yes	X	X
	(-)	X	X	X

In the next section I survey the evidence on the demand for privatization and apply existing explanations, first using the median voter model and then an alternative, the directional theory of voting. Though the directional theory offers some important insights, neither theory is sufficient to explain how privatization appeared on the electoral agenda or why the Conservatives chose the position they did. To explain these two decisions, I turn to supply-side factors, and argue that from personal political advantage and then party political advantage factors a much fuller explanation of the oil asset privatizations can be achieved.

7.1. Public Demand for Privatization

One of the most misunderstood aspects of the privatization phenomenon in Britain is its level of public support. The majority of public opinion was unfavourable to the sale of government industries throughout. These opinions, however, were not intensely held by the British electorate.

Table 7.2. Attitudes Towards Change in Ownership of Specific Industries

Nationalization	Bad Idea	Good Idea
Banks (1976)	76	14
Insurance Companies (1976)	76	15
Privatization	Bad Idea	Good Idea
Water (1989)	75	15
Electricity (1988)	66	24
Electricity (1989)	60	26
Coal Board (1988)	54	34
Steel (1988)	50	38
British Rail (1988)	49	40
British Gas (1985)	47	36
British Telecom (1983)	46	39

Source: MORI poll, May 1976; Gallup polls, November 1983, November 1985, March, August and October 1988; and February 1989.

Public Opinion and Privatization

Information from various opinion polls reveals that privatization was not a popular policy nor an intensely held policy position by the majority of the British electorate, either for or against. The status quo, in fact, was the preferred position as the public was opposed to both Labour plans to nationalize banks and insurance companies in 1976, and Tory plans to denationalize (or privatize) specific companies in the 1980s (see Table 7.2.).

On the issue of government ownership in general, the status quo has been the most favoured policy since the 1960s (see Figure 7.2). From 1966 to 1979 the question the pollsters used was whether there should be 'more nationalization' or 'some denationalization.' Since 1983, the pollsters asked whether 'more should be nationalised/ in public ownership' or 'more should be privatised/sold off.' In all cases, respondents were also given the choice of 'status quo' or 'don't know.' Some differences can be attributed to this change in phrasing from 'some' to 'more' privatization and including public ownership with nationalisation. The *Economist* noted the effect of wording in 1976:

> The bad image surrounding the concept of nationalisation is partly semantic: when questions were asked about public ownership the position improved. For example, only 19% of voters agreed with the statement that "More nationalisation would be good for the country", whereas 35% expressed agreement when the words "public ownership" were substituted.[9]

According to Figure 7.2, the status quo was the preferred position over time, except when 'more should be privatised' slightly surpassed the status quo in 1983. Though there were shifts between 'some nationalisation' and 'more denationalization' those

[9] 'Voters think Its's Codswallop,' *Economist*, 11 September 1976, based an a MORI poll.

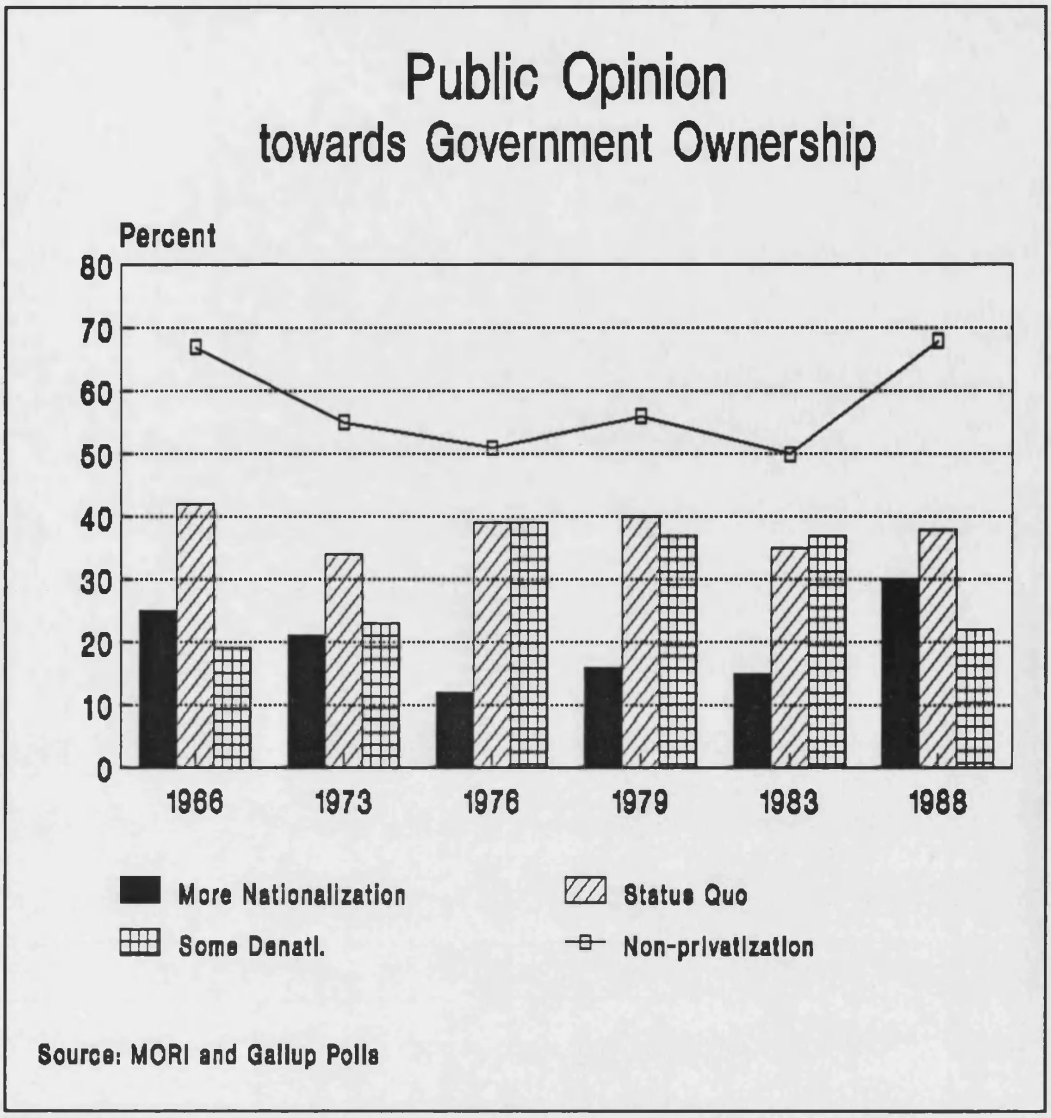


Figure 7.2.

for 'more denationalization' were never greater than those who favoured 'some nationalisation' and the status quo combined, as represented by the line above the bars.[10] When the status quo was not an option and the issue was presented as two-sided, the status quo position split so that opinion was almost perfectly divided with 44 per cent for more privatization and 43 per cent against with 13 per cent having no

[10] The MORI research organization has found that, over time, there has been a 7% shift away from nationalization to denationalization. MORI, *British Public Opinion*, October 1987, p.7.

opinion.[11]

Though there have not been specific measures of intensity of opinion on privatization, its low salience is evident from its poor showing in the only four polls of important issues in which it was mentioned. Public ownership as an issue was only mentioned twice between 1978 and 1987 in the Gallup's monthly poll of most important issues, in 1978 and 1979. Both times it was on the list of the two most important issues, and never on the list of the single most important issue facing the country. In both years, nationalization was eleventh with only 10 per cent of those polled mentioning it, compared to the number one issue, the cost of living, which 68 per cent of those polled mentioned.[12] Its low salience is also evident from the BBC Election Surveys in May 1979 and May 1983. In 1979, nationalization/public ownership was number 13 on the list and only 3 per cent of those polled considered it one of the two most important issues; in 1983 it was again last and this time only 1 per cent of those polled mentioned it.[13] Other polls focusing on the salience of issues and why people voted for one party over another do not even mention privatization/nationalization.[14] Specifically in terms of the sale of oil assets, there were not even any opinion polls asking about the privatization of oil companies,

[11] In December 1984 voters were asked whether they supported or opposed a policy the government could adopt: 'Sell more state-owned industries to private shareholders.' *British Public Opinion*, Vol.VI, No.10, November/December 1984, p.7.

[12] The question was: 'Here is a list of topics that might be discussed at the next General Election. Which, if any, of them do you think should be concentrated on by the politicians?' Gallup Poll, 14-23 December 1979; and December 1978.

[13] The question was: 'Think of all the urgent problems facing the country at the present time. When you decided which way to vote, which TWO issues did you personally consider most importantly?' BBC Election Survey, 11-16 May 1983 and May 1979.

[14] Gallup Polls, 5-11 April 1979; and Abromeit, 'British Privatization Policy,' p.82.

suggesting that the issue was not salient enough to warrant conducting a poll.

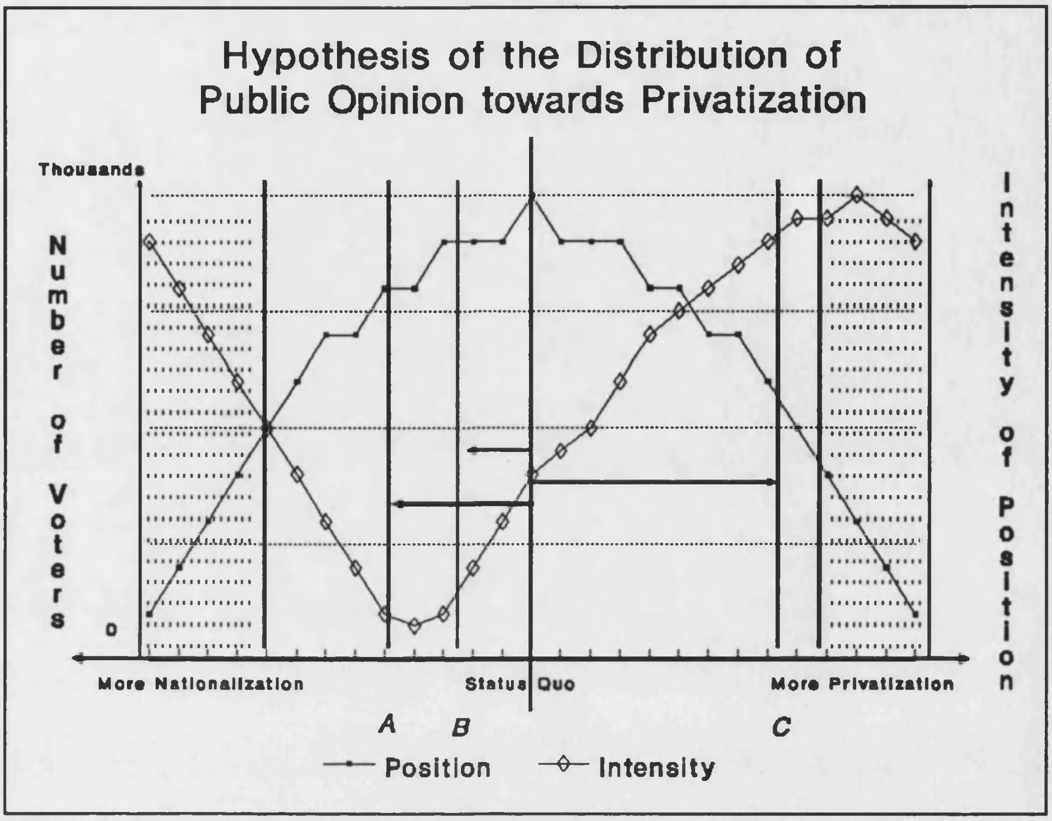


Figure 7.3.

Building from these pieces of evidence, I hypothesize that the distribution of positions regarding privatization during the late 1970s and early 1980s was fairly symmetrical (see Figure 7.3). The Labour and Liberal Democrats' positions were close to the centre with Labour slightly further to the left, point A, than the Liberals, point B, and the Conservatives on the other side of the status quo on the far right, point C. From this distribution, the median voter model, using only the spacial proximity of position, predicts that voters will chose the candidate with the stance closest to their own, which in this case would be the Liberal Democrats followed by Labour, with the Conservatives receiving the least number of votes. Because the Conservatives won both the 1979 and 1983 elections, these predictions hardly seem accurate.

An alternative explanation is suggested by George Rabinowitz and Stuart MacDonald's directional theory of voting. The theory argues that voters react to politicians' direction and intensity on an issue. The direction of the policy is more important than proximity and, therefore, those even slightly favouring privatization will vote for politicians advocating vast privatization rather than a status quo position that is closer but in the opposite direction.[15] While the theory argues candidates are punished for extreme positions outside a 'region of acceptability,' any position within that region is competitive (p.108). The second dimension of the theory is the intensity of opinion. The theory argues that 'if a voter is directionally compatible with a candidate, increasing candidate intensity makes the voter like the candidate more.'(p.101) Thus, the theory suggests that the Conservatives advocated a more extreme position to heighten the importance of the issue.

When the electorate is evenly divided on an issue, as we estimate they were for privatization, the theory predicts that if the candidates are on opposite sides, each gets half of the vote because voters choose according to direction not proximity (p.109). In this case (and directly contradicting the median voter model), the Conservatives would receive half the votes because they were the only party on the right, no matter what their position. Labour and the Liberals, both being on the left would share their half of the votes. The Conservatives' position according to the theory was constrained only by the 'region of acceptability' and the need to raise the level of intensity. Selection of specific positions in these situations, however, 'are virtual lotteries...'(p.115) and chosen according to 'factors such as the state of the

[15] George Rabinowitz and Stuart Elaine MacDonald, 'A Directional Theory of Issue Voting,' *American Political Science Review*, Vol.83, No.1, March 1989, p.114.

times or candidate personality'(p.109) or the preferences of the elites (p.111).

To better understand the position that politicians do chose, we need to relax two of Rabinowitz and MacDonald's assumptions. First, intensity of opinion is not necessarily correlated with the extremity of the position. Voters can feel strongly about a moderate policy position or their opinion may be weak for an extreme position. The implication is that voters will not vote according to an issue if they feel weakly about it - no matter what their position. Second, while voters react to candidates, they also influence candidates. Therefore, instead of the one-way direction of influence Rabinowitz and MacDonald describe, through their intensity on a position, voters can influence the policy position candidates choose. Thus, there is actually a two-way flow of influence.

The case of privatization can better be understood as an issue with a low level of intensity for the majority of the population who therefore voted according to other issues. Though the Conservatives chose progressively more extreme positions, the level of intensity on the issue did not increase sufficiently so that voters reacted. Thus, the politicians were able to select their own policy positions according to other criteria, as discussed in the next section.

The low level of intensity was in fact a key aspect of the politicians' decision making at the time as Nigel Lawson explained in our interview. The absence of strong public feeling was the most important condition he identified and why he felt he was able to initially implement the oil asset privatizations.

> There was no organized lobby. There was a general uneasiness, a fear of what could happen. But also it was nothing that directly touched the man or woman in the street... If a North Sea oil company is going to be privatized it is not something that the man or woman in the street

is going to feel strongly about.[16]

His focus was fear of electoral punishment, not pleasing public demand or gaining votes - at least not in these early privatizations. This lends support to the view that voters do not always respond to stimuli from politicians and that politicians can have other reasons for selecting a policy position.

7.2. Politicians as Policy Suppliers

The development of most policies demands a policy entrepreneur to initiate and promote the ideas.[17] A policy entrepreneur risks the costs and the possibility of policy rejection or the unsuccessful implementation of the policy for the rewards of influence, patronage and social prestige for the successful adoption of his or her policy. There are three sets of costs to initiating a policy: development, information and promotion. The start-up costs are the development costs which include defining and articulating the policy. Then there are the information costs associated with identifying potential supporters and opponents and devising a feasible plan for implementation. Finally there are the promotion costs with include publicizing the policy, either within the party or more broadly, as well as addressing grievances and opposition.

Policy entrepreneurs do not necessarily have to be politicians, though many of the rewards for success are most easily bestowed upon politicians, as was the case with the privatization entrepreneurs in the Conservative party. In the case of the 1977

[16] Interview with Lord Nigel Lawson, 15 February 1994.

[17] Not necessarily the same as a political entrepreneur who organizes political interest groups (Dunleavy, *Democracy, Bureaucracy and Public Choice*, p.34-5), though a policy entrepreneur may chose that strategy.

sale under the Labour party, however, the policy entrepreneurs were BP executives and IMF officials. They took on the cost of promoting the idea, building support and overcoming technical obstacles, such as promoting the sale and arranging the underwriting. Though the final decision was made by Labour politicians, the initial impetus came from outside. But notably, there were no politicians willing to take a personal stand of opposition. To do so they risked their Cabinet seat, one of the prize personal political benefits. The BP sale was a singular case, possibly even a one-off because the sales might not have been sustained if there had not later been Conservative party policy entrepreneurs.

The Prime Minister and Her Strategy

In Britain, many of the personal political benefits are bestowed by the Prime Minister. And because he or she has the power to make ministerial appointments, many MPs initiate policies that are favourable to the Prime Ministers' own strategies in an effort to gain his or her favour and advance their own careers.[18] In addition, because the Prime Minister (PM) has considerable control over the policy-making apparatus, including top level bureaucrats' promotions, the legislative timetable and Cabinet committees, support from the PM is important for the success of the policy. For the case of the oil asset sales, it is therefore necessary to understand the PM's own personal and electoral strategies and how they were affected by privatization. I will then examine the role of four politicians in the development of the oil sales and the subsequent effect on their careers.

Though the extent to which Prime Ministers utilize the resources of office

[18] Gamble, *The Free Economy and the Strong State*, p.110

varies, the Conservative Prime Minister Margaret Thatcher did so rather fully. She sought to control the agenda and further her own ambitions by appointing her close supporters to key Cabinet committee positions,[19] shrouding the budget in secrecy until the morning of the budget speech,[20] and removing or side-lining her most prominent critics.[21] Thus, more so than other Prime Ministers, her own personal and electoral strategies were important influences on the development of other policies. Thatcher's position was strengthened by the Conservatives' disciplined party organization and the British first-past-the-post electoral system which allowed the Conservatives a larger majority than represented by the population.[22] For example, the Conservatives' victory in 1983 was secured with fewer votes than in 1979, yet their parliamentary majority increased by 100 constituency seats to 144.

Thatcher was also well known for consistently rewarding those MPs loyal to her and her strategy. Norman Tebbit recalled that towards the end of 1980, Thatcher

> made it plain that she wanted to begin the reconstruction of the government to bring forward more of those who believed in the policies on which we had been elected,' [or in other words] 'who believed that the policy of government was right and that it could be

[19] Middlemas, *Power, Competition and the State*, p.259; Gamble, *The Free Economy and the Strong State*, p.131; Hugo Young, *One of Us*, pp.142-3 and p.149; James, *British Cabinet Government*, p.169.

[20] House of Commons Treasury and Civil Service Select Committee, Sixth Report, Budgetary Reform, Sixth Report, *British Parliamentary Papers*, 1981-82, HC 137, p.ix; Gamble, *The Free Economy and the Strong State*, p.109; Pliatsky, *The Treasury Under Mrs. Thatcher*, pp.81-5; Hugo Young, *One of Us*, p.149; Holmes, *The First Thatcher Government 1979-83*, p.76; and Prior, *A Balance of Power*, p.119.

[21] Thatcher, *The Downing Street Years*, pp.130-1, pp.152-3; Prior, *A Balance of Power*, p.132; Gamble, *The Free Economy and the Strong State*, p.110; Norman St.John-Stevas, *The Two Cities* (London: Faber and Faber, 1984), p.19; Anthony King, 'Margaret Thatcher as a Political Leader,' in Robert Skidelsky, ed., *Thatcherism* (London: Chatto & Windus, 1988), p.59.

[22] Hugo Young, *One of Us*, p.324.

carried through.[23]

In retrospect, many Conservative politicians have been criticised for allowing Thatcher to proceed unopposed. One of Thatcher's leading adversaries, Jim Prior, defends himself against these criticisms, explaining that though he would have been prepared for the personal setback, he had been elected to represent his constituency and could not let them down.[24] He pointed out that resignation of the whole opposing faction within the Conservative Party

> might have brought down the government. Certainly if all those who had strong disagreement with the policy had resigned, it would have brought down the government. And we were not elected, as it were, to resign and bring down the government. So we stuck in there.[25]

The strategies that Thatcher chose, and therefore, that policy entrepreneurs needed to accommodate, stemmed from her concern with her leadership image.[26] A decade of U-turns had made British voters sceptical of their politicians' ability to stay the course. Thatcher saw this as the cause of Edward Heath's demise: 'It was also irritating that it was because we had done a U-turn with the previous Conservative government that we had lost, because people had lost respect for the government.'[27] She therefore chose to differentiate herself from both the Labour Party and the previous Conservative leadership. She portrayed an image of determination and

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[23] Norman Tebbit, *Upwardly Mobile* (London: Weidenfeld & Nicolson, 1988), pp.9-10 and p.18.

[24] Prior, *A Balance of Power*, pp.140-1.

[25] As quoted from 'Thatcher: The Downing Street Years,' BBC1, 9:30 p.m., 20 November 1993.

[26] Jim Bulpitt, 'The Discipline of the New Democracy: Mrs Thatcher's Domestic Statecraft,' *Political Studies*, Vol.XXXIV, 1986, p.21.

[27] Margaret Thatcher speaking on 'Thatcher: The Downing Street Years.'

strength which emphasized credibility over popularity.[28] Thatcher, in fact, staked her career on providing strong leadership. This came to mean a clear direction for the party without any policy U-turns. While there were benefits to such a strategy, there were also serious consequences; Thatcher set expectations and was then compelled to adhere to her pronouncements at the risk of losing credibility.[29]

Thatcher's overall success is evident from her high favourable ratings as a leader, while the policies she used to establish that profile were not as highly rated by the public (see Figure 7.4). Because the Conservatives won elections in 1979, 1983 and 1987 with Thatcher as their leader, the policies may have only had secondary importance, but there are no polls which measure the relative salience of leadership and issues to confirm this point.

One of the primary means Thatcher, and thus the Conservative Party, used to demonstrate her steadfastness was monetary policy. The changing international situation had made monetary policy an effective policy tool that no party could ignore (see Chapter Four). There was, however, a marked shift in emphasis under Thatcher who used it as a policy weapon capable of producing powerful results.[30] The way

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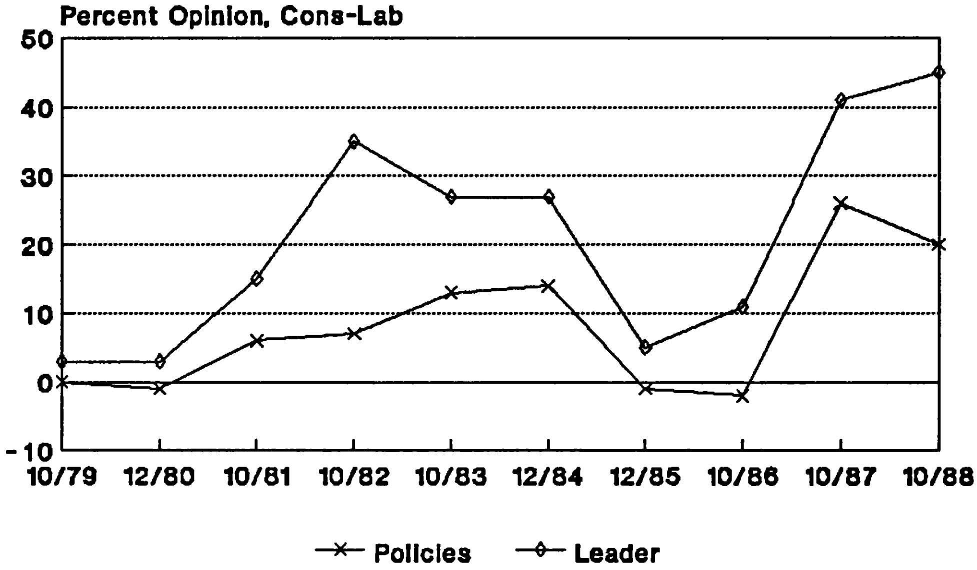
[28] Interview with Lord Home in Patricia Murray, *Margaret Thatcher* (London: W.H. Allen, 1980), p.140; Grant, 'Business Interests and the British Conservative Party,' pp.151-2; Keegan, *Mrs. Thatcher's Experiment*, p.134; and Budge, et. al., *The Changing British Political System*, p.14.

[29] Thatcher, *The Downing Street Years*, p.15 and pp.148-53; Keegan, *Mrs. Thatcher's Experiment*, p.160 and p.183; Francis Pym, *The Politics of Consent* (London: Hamish Hamilton, 1984), p.5 and p.10; Hugo Young, *One of Us*, p.212 and p.319; and a similar version stated by Thatcher on BBC1.

[30] Maurice Wright, 'Big Government in Hard Times: The Restraint of Public Expenditure,' in Christopher Hood and Maurice Wright, eds., *Big Government in Hard Times* (Oxford: Martin Robertson, 1981), p.9; Browning, *The Treasury and Economic Policy 1964-1985*, pp.264-287; Riddell, *The Thatcher Decade*, pp.16-7; and Ranelagh, *Thatcher's People*, p.226.

Figure 7.4. Public Opinion, 1979-88
Conservatives Favoured Over Labour



Source: Gallup Polls, 1979-88.

monetarism was used to ensure financial confidence was by enhancing stability and forcing the government to act predictably, rather than engineering carefully timed changes through policy actions.[31] In other words, its success depended on the government's unflagging commitment to the policy over time.[32] One of the means the government devised to build the financial market's confidence was the Medium Term Financial Strategy (MTFS), a statement of intermediate range targets including the PSBR.[33] Given the difficulty in forecasting the PSBR, many economists have noted that it is surprising that it remained a central plank of the government's

[31] Alan Meltzer, 'Monetarism,' in David Henderson, ed., *The Fortune Encyclopedia of Economics* (New York: Warner Books, 1993), p.131; Keegan, *Mrs. Thatcher's Experiment*, pp.65-6; and Lawson, *The View from No.11*, p.90 and p.414.

[32] Gardner, *Decade of Discontent*, p.90.

[33] Holmes, *The First Thatcher Government 1979-83*, p.105; and Hillman and Clarke, *Geoffrey Howe*, p.146.

strategy.[34] It did, however, continue to be of great importance and public attention, therefore, focused upon it.

The problem with this strategy was that the government failed to meet the targets, yet could not afford the credibility repercussions by admitting it.[35] Privatization as a means to help meet the PSBR target was, therefore, a welcome policy initiative, and those who developed it were well rewarded by Thatcher. Although the Treasury could 'fiddle the figures' (see Chapter Six) and the Bank of England could overfund the debt,[36] these measures were primarily cosmetic.[37] The real contributions were politically difficult - such as cutting spending or raising taxes. Privatization provided another method of reducing the PSBR which had the same affect as cutting spending, and was therefore very appealing to both the politicians

[34] Morris, 'Budgetary Arithmetic and the 1982 Budget,' p.99; Devereux and Morris, 'Budgetary Arithmetic and the 1983 Budget,' p.39 and p.42; and Devereux et al., *Budget Options for 1984*, p.38.

[35] As quoted in C. Johnson, *The Economy Under Mrs Thatcher 1979-1990*, p.68.

[36] Funding the debt means selling medium and long term government debt (more commonly called gilts) to the non-bank public. Overfunding essentially means selling more government securities to the investing public than is necessary to meet the government's own requirements. Scholars and civil servants and even Nigel Lawson have noted that a significant amount of overfunding occurred in 1981-82 and again in 1983-84. Professor Kaldor, in evidence to the Treasury Select Committee, produced impressive evidence that most of the growth in Britain's money supply was the result of bank advances. The gilts, of course, had to be paid back, which caused greater spending pressure in the future. Pliatsky, *The Treasury Under Mrs. Thatcher*, p.126; Lawson, *The View from No.11*, pp.448-9 and p.458; and Browning, *The Treasury and Economic Policy 1964-1985*, p.294.

[37] Even the Labour government (1974-79) pursued devious means to achieve monetary targets. The Labour Minister Harold Lever used 'ripping wheezes' to achieve a reduction in the PSBR, by persuading the clearing banks and later the Trustee Savings Bank (TSB) to re-finance export credit and shipbuilding, and to finance local authority mortgages. Lever did the same with Housing Associations, which were being financed through the National Loan Fund. Lever created a private limited company, the Housing Corporation, through which government grants were then channelled. When the company borrowed from the banks it did not count as public expenditure of PSBR, even though guaranteed by the government. Likierman, *Public Expenditure*, pp.9-10.

who had staked their credibility on monetary policy and the Treasury whose reputation was under question (as described in Chapter Six).

The way privatization worked was that an asset sale simply allowed expenditure (or cuts in taxation) in the current period, beyond the extent feasible without it, by raising current income at the expense of future income streams.[38] If the marginal increase in spending were less than was actually raised from the sale, the PSBR would be lower, all other things being equal. With an asset sale, however, the PSBR would be larger in future years unless the sale price reflected the loss of revenue to the government in the form of current and future profit and if the government used the sale proceeds to purchase other financial assets providing a similar yield or to retire an equivalent amount of outstanding debt.[39] The British government, however, often used the proceeds from asset sales to offset increased spending which continued to increase from 1977 to 1989.[40]

Both the Labour Party in 1977 and the Conservatives after 1979 used privatization as a means to achieve PSBR targets. The Cabinet discussions of the Labour government in 1976 during the IMF crisis illustrate why cutting the PSBR was important but spending cuts were difficult for political reasons (see Chapter Three). Similarly, the Conservatives entered office in 1979 having made too many promises to cut the PSBR on the one hand, and too many promises to increase spending on the other. The sale of BP shares was particularly important in 1979 and

[38] Ali Mansoor, 'Budgetary Impact of Privatization,' p.4; and Gamble, *The Free Economy and the Strong State*, p.124 and p.250.

[39] Richard Hemming and Ali Mansoor, 'Privatization and Public Enterprises,' IMF Occasional Paper No.56, January 1988, p.16; and Mansoor, 'Budgetary Impact of Privatization,' p.5.

[40] Central Statistics Office, *The Government's Expenditure Plans*, 1977-90.

1983 to help the Conservative government achieve its rigorous spending reductions in the least harmful way.[41] Asset sales soon became a regular part of the Conservatives' budget planning. In fact, asset proceeds were posted in the preceding year's budget, creating high risks if the government failed to deliver. Failing to reach privatization receipt targets would have negative budgetary as well as political credibility consequences, which explains why some privatizations proceeded in the face of difficulties and complications.[42]

Privatization proceeds were the first major contributions to reducing the PSBR while at the same time maintaining the spirit of the MTFS.[43] Leo Pliatsky, a former Treasury civil servant explained the electoral advantages of this:

> The government's supporters found some consolation for this setback [inability to cut public spending] in the better than expected success of the programme of privatization of publicly owned industries and companies and disposals of publicly owned assets; this form of cutting the public sector became to some extent a kind of psychological substitute for cutting public expenditure. The receipts from these sales also brought some material help to the government's accounts.[44]

Oil may have been the largest contributor to the government's revenues as sales of oil assets were the largest individual contributor to privatization and oil revenues from the North Sea began to dwarf the PSBR by 1984. The effect of total privatization and oil revenues from the North Sea from 1977 to 1989 is illustrated in Figure 7.5 as compared to the PSBR; it should also be noted that expenditure was

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[41] Lawson, *The View from No.11*, p.34 and p.284.

[42] Letwin, *Privatising the World*, p.41; and Gamble, *The Free Economy and the Strong State*, p.131.

[43] Keegan, *Mr. Lawson's Gamble*, p.94.

[44] Pliatsky, *The Treasury Under Mrs. Thatcher*, p.210; also see C. Johnson, *The Economy Under Mrs Thatcher*, p.173.

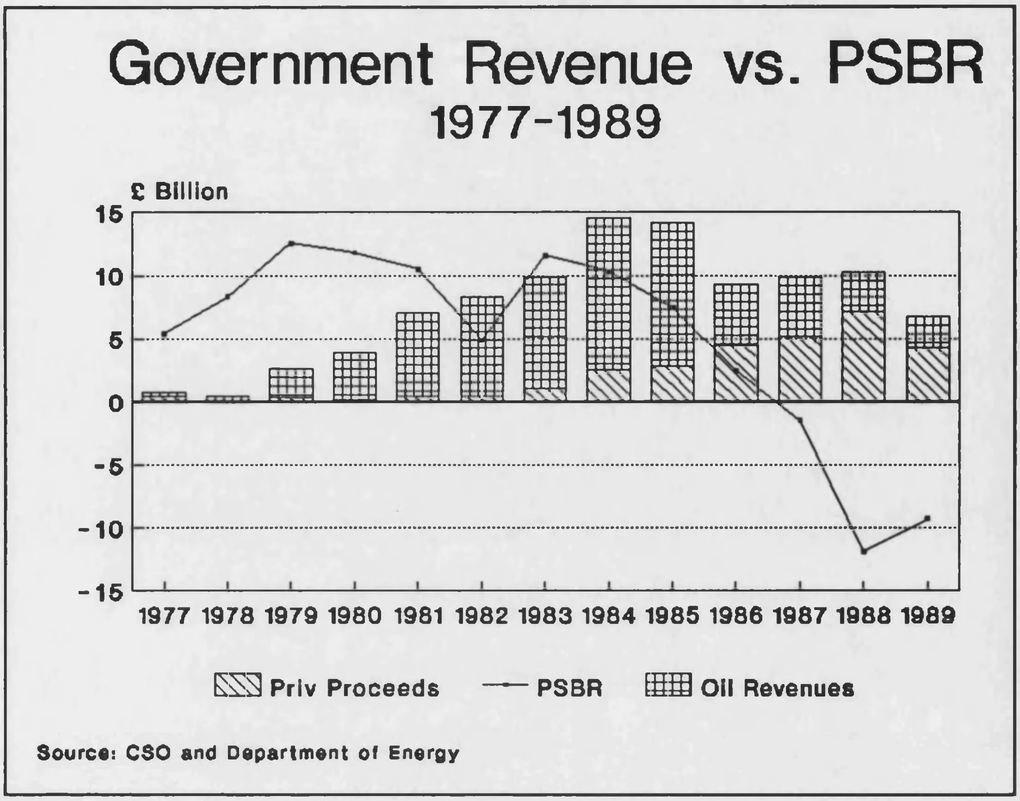

Figure 7.5.

increasing throughout the period. Privatization proceeds rose steadily through 1988, while oil revenues peaked in 1984 and began to fall as the price of oil collapsed in 1986.

Policy Entrepreneurs - Successes and Failures

With these advantages, privatization, especially of oil assets, was useful to Thatcher and thus the Conservative's overall political strategy. Though Thatcher was not an initial supporter of privatization, once she was shown the political virtues of the policy,[45] she supported it wholeheartedly.[46] In addition, those who successfully carried the initial costs and risks of policy development were well rewarded by Thatcher with public recognition and promotion. I review the case of four Conservative politicians, Nigel Lawson, John Moore, David Howell and Hamish Gray, and examine their entrepreneurship and corresponding rewards.

Nigel Lawson was one of Thatcher's most important lieutenants. As Chief Financial Secretary to the Treasury in 1979, Nigel Lawson's career advancement and personal credibility were bound up in the government's commitment to the MTFS.[47] He approached privatization from the political perspective, seeking revenues to meet the government's targets, and thus advocated the sale of Amersham International in 1980. When the sale was 24 times oversubscribed, it appeared he had gambled to ensure it was a political success and lost some personal credibility. Lawson recorded the implications in his memoirs:

> at the time I felt deeply humiliated, and resolved that the next privatization for which I was responsible, namely Britoil, would have to be a tender. Whatever happened, I could not afford a second Amersham.[48]

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[45] Lawson, *The View from No.11*, p.199; and interview with Department of Energy civil servant.

[46] Thatcher, *The Downing Street Years*, pp.677-8.

[47] Keegan, *Mr. Lawson's Gamble*, p.60 and pp.70-2; and Holmes, *The First Thatcher Government 1979-83*, p.62.

[48] Lawson, *The View from No.11*, p.210.

As Secretary of Energy from 1981 to 1983, Lawson was the driving force behind the DEn's privatizations. He wrote the 1981 Oil and Gas (Enterprise) Bill, got it passed, privatized Britoil and prepared Enterprise Oil for sale.[49] One civil servant thought that Lawson was self-serving and only trying to improve his ministerial image: because Howell had been so indecisive, Lawson saw that 'the easy way to look good was to make a move.'[50] It was also perceived at this time that his advocacy of privatization might also be seen as a means of raising revenue to cut the PSBR to ensure that his MTFS targets were met.[51] The oil privatizations were especially important to Lawson. As a policy entrepreneur and a young member of Thatcher's Cabinet moving to the Department of Energy, which was not one of the most sought after posts, he had to work with what was available to make his mark. Oil was especially important to Lawson because other types of energy - coal, electricity, nuclear, even gas - involved too many obstacles, so much so that none were even targeted for privatization in the Conservative's 1983 manifesto.[52] Lawson accords the oil asset privatizations three chapters and oil a further chapter in the eleven chapters of his memoirs devoted to his experience as Secretary of State for Energy; the first one was even titled: 'Jewel in the Crown.'[53]

For taking an entrepreneurial risk, Lawson was rewarded with policy success,

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[49] Interview with Conservative minister.

[50] Interview with Department of Energy civil servant.

[51] Adrian Hamilton, *Times*, October 1981, as quoted in Keegan, *Mr. Lawson's Gamble*, pp.94-5.

[52] Conservative Party, 'The Challenge of Our Times,' 1983 Manifesto, pp.16-7.

[53] Lawson, *The View from No.11*. The 1987 BP share sale received a further two chapters in Part IV of his memoirs.

and his abilities and loyalty were much appreciated by Thatcher. She promoted him from Energy to Chancellor of the Exchequer after the Conservatives won the 1983 election, recording her regard for him in her memoirs:

> Whatever quarrels we were to have later, if it comes to drawing up a list of conservative - even Thatcherite - revolutionaries I would never deny Nigel a leading place on it. He has many qualities which I admire and some which I do not. He is imaginative, fearless and - on paper at least - eloquently persuasive. His mind is quick and, unlike Geoffrey Howe who he succeeded as Chancellor, he makes decisions easily....I doubt whether any other Financial Secretary to the Treasury could have come up with the inspired clarity of the Medium Term Financial Strategy which guided our economic policy.[54]

Another Conservative minister who made political capital out of privatization was **John Moore**. As Parliamentary Under Secretary in the DEn, he was in charge of the sale of Amersham in 1980, and involved in the Britoil and Wytch Farm sales.[55] In 1983, Moore was chosen to head the new Treasury unit overseeing the privatization programme as a whole as the policy became a central part of the Conservative programme.[56] Moore was cast as a trailblazer and Thatcher rewarded him with successive appointments to the posts of Secretary of State for Transportation in 1986, Social Services in 1987, and Social Security in 1988.

David Howell's handling of privatization provides an example of an unsuccessful policy entrepreneur. As one of the original architects of 'Thatcherism' and an author of *The Right Approach* and the 1979 and 1983 manifestos, David Howell also initially gained recognition for his work developing Thatcherite ideas.

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[54] Thatcher, *The Downing Street Years*, pp.308-9.

[55] Interview with Conservative minister.

[56] Riddell, *The Thatcher Decade*, p.92; Pliatsky, *The Treasury Under Mrs. Thatcher*, p.110; and Abromeit, 'British Privatization Policy,' p.72.

Appointed to the Cabinet in 1979 as Secretary of State for Energy, he was unsuccessful in turning the idea of privatization into a concrete policy. Howell drew up the original studies on privatization and wrote a draft bill to privatize BNOC. He instructed the British Gas Corporation (BGC) to sell Wytch Farm (under the 1972 Gas Act),[57] but he never got the Bill passed or completed a privatization. The reason, according to a fellow minister, was that he 'could come up with 440 ways to answer a question but could not make a decision. The thinking was initiated under Howell, but things didn't get done.'[58] According to a DEn civil servant the delay in privatizing BNOC from 1979 to 1982 could specifically be attributed to Howell's indecisive personality.[59]

As well as stepping back from privatization, he did not perform well in crises, particularly the threatened coal strike in 1980. He also muddled the DEn's oil depletion policy and created additional problems over gas and electricity prices. One civil servant stated simply, 'it was embarrassing.'[60] Howell was moved to head the Department of Transport in the September 1981 Cabinet reshuffle, and was dropped

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[57] Many of the civil servants I interviewed had to think for a few minutes before recalling that Howell did start the privatization process. They all pointed to the fact that it was actually Lawson who got them going, and therefore, Howell's contribution paled in comparison. Interviews with Department of Energy minister and civil servants.

[58] Interview with Conservative minister.

[59] Interview with Department of Energy civil servant.

[60] A Conservative minister claimed that Howell was one of the first proponents of privatization advocating it as early as 1970 in his pamphlet, 'New Style of Government' published by the Conservative Political Centre. Interview with Conservative minister; Hillman and Clarke, *Geoffrey Howe*, p.71; Adrian Hamilton, 'Mr. Lawson Starts the Big North Sea Sell Off,' *Times*, 20 October 1981; Thatcher, *The Downing Street Years*, p.142 and p.151; Lawson, *The View from No.11*, p.185; Middlemas, *Power, Competition and the State*, p.249; and interviews with Department of Energy civil servant and BNOC executive.

from the Cabinet after the 1983 election.[61] Competence as well as ideas were necessary to successfully create a policy in Thatcher's Cabinet.

Hamish Gray is an example of a Conservative minister failing to support Thatcher's policies or propose more successful alternatives. As a Scottish MP and Minister of State for the Department of Energy Gray sought to direct benefits to Scotland in general and his constituency in particular, through government involvement in the oil industry. He advocated keeping BNOC. He also supported the DEn's gas pipeline proposal as well as the department's plans for depletion policy, all of which would have aided the future of the Scottish oil and gas industry. These issues, however, found little favour with Lawson and Thatcher, and all were eventually defeated, except for the retention of BNOC's trading operation.[62] Gray was not a policy entrepreneur, but a policy realist with limited aims. After gaining the concession that it would remain in Scotland, he withdrew his opposition to the sale of Britoil. As one civil servant explained:

> Gray was an old school Tory. He was pragmatic; he didn't argue for change. But he did not die in a last ditch effort to prevent change, and didn't have the power to do so anyway.[63]

He was described by a Conservative minister as 'a pair of safe hands. He saw that privatization was right, but that it was difficult. He would never have ventured out on it on his own.'[64] Gray lost his seat in the 1983 election, but because of his

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[61] Thatcher, *The Downing Street Years*, p.142 and p.151; and Middlemas, *Power, Competition and the State*, p.249.

[62] Lawson, *The View from No.11*, p.184; and interviews with Department of Energy civil servant and minister.

[63] Interview with Department of Energy civil servant.

[64] Interview with Conservative minister.

Scottish base, he was made a Lord and appointed to the Scottish Office for two years. Ministers pointed out, however, that the Scottish Office was not nearly as interesting or as prestigious as the DEn.[65]

7.3. Party Political Advantage for the Conservatives

There are two dimensions to party political advantage. The first is a cost-benefit analysis which computes the costs and benefits for supporters and opponents over the short and long-term. A positive outcome influences party leaders to place the issue on the political agenda. The second dimension is the distribution and intensity of Conservative voters on the issue. By calculating the demand within the party, leaders can determine the position of greatest advantage.

The Cost-Benefit Analysis

The supply side calculation of electoral advantage, for policies without strong demand factors, includes the distribution of costs and benefits and the time horizon of their impact, see Figure 7.6.[66] Politicians and parties seek policies that will target benefits towards their supporters. Because it is not fruitful for politicians to pursue policies that do not have benefits for their supporters, the table does not consider such options. While benefits ideally go to supporters, costs ideally go to opponents. The time horizon of costs and benefits are especially important to politicians as the electoral cycle means they may not be in office for the long-term. Therefore,

[65] Interview with Department of Energy ministers.

[66] James Q. Wilson, *Political Organization*, 1973, chapter 16 as discussed in Dunleavy and O'Leary, *Theories of the State The Politics of Liberal Democracy*, pp.110-11.

Figure 7.6. Electoral Analysis Cost-Benefit Concentration and Time Horizon	Benefits Target Supporters (all cases)	
	Short-term	Long-term
Costs Target Supporters - Concentrated or Dispersed		
Short-term	**Do Nothing** 1	**Do Nothing** 2
Long-term	**Be Very Careful** 3	**Do Nothing** 4
Costs Target Opponents - Concentrated		
Short-term	**Be Very Careful** 5	**Do Nothing** 6
Long-term	**Be Careful** 7	**Be Careful** 8
Costs Target Opponents - Dispersed		
Short-term	**Be Careful** 9	**Be Careful** 10
Long-term	**Act Fast** 11	**Act Fast** 12

benefits which can be achieved in the short-term are the most attractive, so that the politicians in power can receive credit for the benefits. Conversely, costs which can be delayed beyond the next election are the most desirable.

The possible variations of the concentration of costs and the time horizon are the key factors that determine how easy and how worthwhile a policy is to pursue. The concentration of costs means recipients cannot afford to ignore them and are better off taking on the costs of opposing the action. The more concentrated the costs, the less likely there will be a free-rider problem and the more likely opposition will be co-ordinated and effective. Should costs go to supporters, for example in a situation where costs are dispersed and the impact is subtle (boxes 1-4), it is only worthwhile to proceed if they are felt in the long-term, and even then it is a risky strategy (box 3). If costs are targeted to opponents and concentrated, politicians need to proceed very carefully with the policy, especially if concentrated in the short-term, (box 5). If the benefits in this case accrue to supporters in the long-term, the policy is not worth the risk (box 6). However, if the effect of the costs are felt by opponents in the long-term, the policy may be worth pursuing carefully (boxes 7 and 8).

When costs target opponents and are dispersed, collective action problems are raised and the risk of opposition is reduced, and therefore the appeal of the policy increases. When the costs are felt in the short-term, there is still need for caution (boxes 9 and 10) but worth the risk because benefits go to supporters. When the costs are dispersed among opponents in the longer-term, this is the ideal situation for a party and the politicians should therefore act fast and implement the policy (boxes 11 and 12).

The change in the Conservatives' stance on privatization from one of caution to one of action can be understood as the movement between the boxes in Figure 7.6. The Conservative's initial delay in privatizing the oil assets can be explained by the perception that there would be a high cost to the sales in the short-term. The government feared they would be caught in an oil crisis and suffer from oil shortages and high prices because they would not have control of their own resources. At this point ministers feared that the costs of privatization would be large in the short-term, and that they would be dispersed among both opponents and supporters (box 1 of Figure 7.6). DEn civil servants pointed to the weight ministers gave to public concern over control of the North Sea; as one stated: 'Ministers saw that it would be politically indefensible to have North Sea oil and still suffer from an oil shortage.'[67]

[67] Interviews with Department of Energy civil servants.

Despite Thatcher, Moore and Lawson's retrospective claims that privatization was part of the Conservatives' plan all along and ministers' claims that privatization was spelled out in the 1979 manifesto, there were only vague references to privatization at this stage,[68] and the accounts of the decision making process for the sale of BNOC and other early privatization by ministers and civil servants clearly reveal hesitation over the policy and an ad hoc beginning.[69] Thus, even though David Howell acted as a policy entrepreneur developing the policy, there was initially no action.

There are several pieces of evidence that illustrate the government's hesitation and lack of commitment to the policy. In 1980 Prime Minister Thatcher was concerned about retaining national control of the North Sea and rejected a number of BNOC privatization options on these grounds at an important meeting of the Cabinet's Economic Committee.[70] A Conservative minister described the slow process in 1979 and 1980 of finding a workable policy for oil privatization:

> In 1980, no one was in favour of selling oil assets. There was little support from other ministers or from Number 10. I could not even persuade Thatcher that it was a good idea. At that time no one had begun to see wider share ownership or privatization as the effective political weapon that it was.[71]

In 1981 Thatcher again hesitated either for political reasons or because of the

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[68] Interviews with Department of Energy civil servants and minister; and Conservative Party, 'The Conservative Manifesto 1979,' 1979.

[69] Thatcher, *The Downing Street Years*, p.688; and S. Young, 'The Nature of Privatisation in Britain, 1979-85,' *West European Politics*, Vol.9.

[70] Interviews with Department of Energy ministers; and Lawson, *The View from No.11*, p.217.

[71] Interview with Department of Energy minister; also see *Hansard Parliamentary Debates (Lords)*, 9 October 1980, vol.413, col.708-710; and 'BNOC: Up for Grabs,' *Economist*, 4 October 1980, p.63.

complications raised by BNOC executives, and through her control of the legislative timetable, was able to prevent the proposed Bill from getting a slot to debate in Parliament that year.[72]

In addition, BNOC chairman Frank Kearton was replaced by an interim chairman in 1980 instead of a pro-privatization chairman. According to other BNOC executives, the government had not yet decided what its policy was going to be.[73] Similarly, Denis Rooke was re-appointed as chairman of BGC in 1980 by David Howell in part because privatization was not yet on the agenda.[74] Civil servants reinforced the initial uncertainty and lack of action. They thought that the denationalization of BNOC was a fait-accompli when the Conservatives arrived in office. Instead, civil servants were surprised by the numerous alternative options that were considered including the sale of exploration acreage and forward sales of oil.[75]

Most importantly, there was no structural evidence within the government of a privatization programme until 1982-83, and thus, until then, it was only a piece-meal response to other problems. For example, the CPRS was not commissioned until 1982 to review the 'state monopolies' and consider the case for returning them to private ownership. And the privatization unit in the Treasury was not set up until

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[72] Interviews with Department of Energy ministers and civil servants and BNOC executive; Boon Philips, 'BNOC Shares Sale Runs Out of Time,' *Times*, 26 March 1981, p.19; David Steel and David Heald, 'Report: Privatizing Public Enterprise: An Analysis of the Government's Case,' *Political Quarterly*, Vol.53, No.3, July-Sept 1982, p.333; and Veljanovski, *Selling the State*, p.65.

[73] Interviews with BNOC executives and CPRS official.

[74] Interview with Lord Nigel Lawson, 15 February 1994. Though others argued that Howell underestimated his ability to convince Rooke of the advantages of privatization. Interview with Department of Energy minister.

[75] Interviews with BNOC executive, Department of Energy civil servants and minister.

1983.[76] Thus, most civil servants recognized that the privatization policy grew in importance over time, while the more cynical thought that the Conservatives had 'stumbled' upon it.[77]

By the early 1980s, the Conservatives realized that instead of potential immediate costs they realized they were in a situation where the costs would occur in the long run and the benefits would accrue immediately (they were therefore no longer in boxes 1-4). The primary change was in the structure of the international oil industry. As discussed in Chapter Four, the industry had become a free-market by the end of the 1980s making state-ownership less necessary and less effective. This was clearly recognized by politicians and Nigel Lawson recalled discussing the reduction in BP's effectiveness:

> She [Thatcher] recalled, or I reminded her, that during the original problems in the Middle East, it was easier to persuade Shell than it was BP, even though we had a majority shareholding in BP at the time.[78]

With potential costs to supporters minimized, the other important factors in the calculation became the short-term benefits of privatization to supporters and short-term costs to opponents. The short-term benefits to supporters included, its contribution to MTFS targets and the promised economic revival,[79] its visibility as

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[76] Blackstone and Plowden, *Inside the Think Tank*, p.83; Riddell, *The Thatcher Decade*, p.92; Pliatsky, *The Treasury Under Mrs. Thatcher*, p.110.

[77] Interviews with Department of Energy civil servants.

[78] Interview with Lord Nigel Lawson, 15 February 1994.

[79] Middlemas, *Power, Competition and the State*, p.249.

a successfully implemented policy and one that received international attention,[80] and its elimination of the need for the party to achieve its electoral promise of disciplining the nationalized industries, which they had been unable to achieve thus far.[81] As such, privatization provided a morale boost to the party which had few policy successes and was unable to agree on many aspects of economic policy.

The main attraction of the oil asset sales, however, was the cash benefit, and all other objectives were secondary.[82] Philip Shelbourne, the chairman of BNOC, spelt out the government's priority: 'The government was even more keen to raise money than we were.'[83] This money enabled the government to maintain spending and eventually offer tax cuts to their supporters. In addition, both Labour and the Liberals opposed privatization, which as Nigel Lawson pointed out,

> is not a bad thing because it helps to keep your own in line. If they think others are opposed, there must be a good reason to support it.[84]

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[80] Keegan, *Mr. Lawson's Gamble*, pp.174-7; McAllister and Studlar, 'Popular Versus Elite Views of Privatization,' p.174; and Wolfe, 'State Power and Ideology in Britain:,' p.248.

[81] Pliatsky, *Getting and Spending*, pp.199-100; Hillman and Clarke, *Geoffrey Howe*, footnote p.82; John Redwood as quoted in C. Johnson, *The Economy Under Mrs Thatcher*, p.154; and interview with Department of Energy civil servant.

[82] Vickers and Yarrow, *Privatization: An Economic Analysis*, p.428; Abromeit, 'British Privatization Policy,' p.83; Dennis Swann, *The Retreat of the State: Deregulation and Privatization in the United Kingdom and the United States* (London: Harvester Wheatsheaf, 1988), p.316; and Dexter Whitfield, *Making it Public: Evidence and Action Against Privatization* (London: Pluto Press, 1983), p.39.

[83] Interview with BNOC executive. Ironically, privatization was actually a U-turn in the Government's monetarist policy. The sales were an easy means to circumvent the fiscal constraints, which were set by the money supply targets which were the core of monetarism. However, because privatization was not presented as such, this contradiction was generally overlooked. Abromeit, 'British Privatization Policy,' p.84.

[84] Interview with Lord Nigel Lawson, 15 February 1994; Keegan, *Mr. Lawson's Gamble*, pp.174-7; McAllister and Studlar, 'Popular Versus Elite Views of Privatization,' p.174; and Wolfe, 'State Power and Ideology in Britain,' p.248.

In terms of the oil privatization, the sales also enabled the Conservatives to direct benefits to specific supporters, namely the oil industry and the financial community. These were two groups of traditional Conservative supporters, and two industries courted by the Conservatives. During the 1979 election campaign and into the Conservative's first term, the management of some private oil companies complained that BNOC was a time consuming and costly irrelevance, while others charged that BNOC was unfair and threatened their rights. As one observer noted, 'BNOC was doomed once the Conservatives came to power.'[85] The Conservatives responded by declaring their opposition to the state owned oil company starting in 1975.[86]

The support of the oil companies was crucial to the Conservatives, but also to any British government because development of the North Sea depended on private investment and expertise. In the early 1980s, there was a lull in North Sea investment (see Chapter Five). One way the Conservative government tried to encourage more industry involvement was to guarantee less government involvement in the industry. Nigel Lawson explained the oil companies reaction to the proposed sale of BNOC:

> They were pleased to see it [the privatization of BNOC] in the sense that the Conservative government had only been in office for three years at that point and was unpopular so they had concerns in the back of their minds as to how a future Labour government might use BNOC. But because the rump remained and it was perhaps something a future Labour government could use it didn't matter as much.[87]

Thus, the sale of BNOC was only an indication of the Conservative's intentions and

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[85] Interview with Department of Energy civil servants and CPRS official; and Middlemas, *Power, Competition and the State*, p.357.

[86] Ronald Fox, 'Oil Denationalization Pledge,' *Times*, 19 September 1975, p.2.

[87] Interview with Lord Nigel Lawson, 15 February 1994.

did not address the most important factor for the oil companies, which was the tax regime.[88] But because the oil companies push for lower taxes on oil from the North Sea clashed directly with the government's need to address its financial problems, the sale of BNOC was a much easier way to try and appease the oil companies.[89] The retention of the trading portion of BNOC, however, reveals the lower priority ministers assigned to appeasing the oil companies.

The financial press supported the government's plans to sell its oil assets. A typical statement from *The Economist*, for example, described BNOC as 'a free-spending drain on the public purse [which] was given excessive privileges by its socialist creators.'[90] The benefits to the financial community were through privatization in general and not specific to the oil sales, as they helped the City of London as well as advertising and public relations firms through a lean time.[91] The payments for such services for the oil sales alone were at least £224 million (see Chapter Three, Table 3.1.).

In addition to the benefits to supporters, the oil sales also targeted costs to their opponents in the short-term. The Conservative's privatization programme wrong-footed the Labour Party, undermining their already weak opposition.[92] Traditional

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[88] Interview with Britoil executive.

[89] Robinson, 'The Errors of North Sea Policy,' pp.29-30.

[90] *Economist*, 12 June 1982, p.516; also survey of articles in the *Financial Times* and *Economist* from 1976 to 1987.

[91] Chapman, *Selling the Family Silver*, pp.67-9; and Whitfield, *Making it Public*, p.39.

[92] The Labour Party was fragmented and disorganized, which was exacerbated by the formation of a new party, the Social Democrats. This divided the opposition limited their effectiveness in Parliament, and according to some scholars, enabled the Conservatives to win the 1983 election. Pliatsky, *Getting and Spending*, p.214; Robert Skidelsky, 'Introduction,' in Robert Skidelsky, ed., *Thatcherism* (London: Chatto & Windus, 1988), p.26; 'Labour

Labour Party disagreement on the nationalization - denationalization issue made it a divisive issue within the Party and hampered the formulation of a convincing alternative programme.[93] The fact that Labour ministers had been the first to privatize oil assets made it additionally difficult for the Shadow Cabinet to oppose the Conservatives' policy on BP. One minister admitted that 'the BP sale set the tone for the Conservative government in 1979, and it was hard to argue with the accounting practice we had set up, which also gave the Conservatives the grounds for further privatization.'[94] Lawson also noted: 'The previous Labour government had inadvertently paved the way with its 1977 BP share sale. So the official Opposition could hardly complain with much conviction.'[95] Another minister recalled gleefully, 'the Conservatives taunted Labour with it later.'[96]

Disagreement in Labour's ranks also emerged in public over the first Britoil sale. The shadow energy spokesman, Merlyn Rees, stated in November 1981 that a Labour government would buy back Britoil at its market price. Shortly thereafter, Tony Benn made a speech contradicting Rees' statement saying the government would

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Party Fragmented,' *Economist*, 6 October 1979; Gamble, p.108; Peter Jenkins, *Mrs. Thatcher's Revolution, The Ending of the Socialist Era* (London: Jonathan Cape, 1987), pp.102-129; Budge et at., *The Changing British Political System*, pp.70-1; Hugo Young, *One of Us*, pp.293-4; Prior, *A Balance of Power*, p.153; and Ivor Crewe, 'The Decline of labour and the decline of Labour: Social and Electoral Trends in Post-War Britain,' Essex Papers in Politics and Government, Number 65, September 1989.

[93] Abromeit, 'British Privatization Policy,' p.72.

[94] Interview with Labour minister.

[95] Lawson, *The View from No.11*, p.34 and pp.199-200.

[96] Interview with Conservative minister.

confiscate Britoil.[97] As Lawson described it: 'The Conservative benches had been on the defensive for so long over unemployment and the economy that they were hugely cheered by Labour's obvious discomfiture.'[98] And though there was a trade union member on the Board of BNOC, there was nothing he could effectively achieve.[99] In addition, the Conservatives were able to diffuse the effectiveness of Labour's opposition against Enterprise Oil by recalling the fact that Labour had tried to separate the oil assets of the BGC so they could be given to BNOC in 1975, but the Labour government retreated in the face of BGC's protests. Pointing to this attempt, the Minister of State for Energy Alick Buchanan-Smith asserted that even the Labour government found it questionable that BGC should be involved in oil exploration.[100]

Though privatization was used as a means to break a trade union stronghold in some cases,[101] the trade unions were not a factor with the oil sales because trade unions were not prominent in the capital intensive oil industry. The employees of BNOC and BGC, however, proved to be strong opponents of privatization. The Conservatives sought to diffuse employee opposition by making employee ownership easy and profitable.[102] A DEn minister pointed out:

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[97] Julian Haviland and Philip Webster, 'Rees Threat to Resign Over Benn's Oil Speech,' *Times*, 11 November 1981, p.1.

[98] Lawson, *The View from No.11*, p.212.

[99] Interview with BNOC board member.

[100] Bailey, 'Unequal Shares in the North Sea,' p.329; and *Hansard Parliamentary Debates (Commons)*, 13 March 1984, col.343.

[101] Lawson, *The View from No.11*, p.437; Ranelagh, *Thatcher's People*, p.223; and Dobek, 'Privatization as a Political Priority,' pp.36-38.

[102] Madsen Pirie, *Micropolitics* (Aldershot: Wildwood House, 1988), pp.187-93.

> There was never any representation from the work force to be nationalized again. In fact many employees increased their share. To ensure that the British people got a reasonable way to participate, we made a special provision for those who worked in the industry, and limited the percentage holding by institutions.[103]

Realizing the short-term benefits yet fearing some of the costs were concentrated towards their opponents (boxes 5 and 7 of Figure 7.6), the Conservatives decided to proceed cautiously but sought to avoid criticism wherever possible. The sensitivity of Conservative ministers to public opinion is evident in many of the specifics of the sales, as strong opposition was purposely avoided, specifically measures that threatened security of supply.[104]

The largest public outcry against privatization occurred when a radical CPRS report was leaked to the *Economist*. The public outcry over severe privatization measures, including privatizing the National Health Service, caused the Conservatives to recoil. Hugo Young, a newspaper reporter at the time, described the Cabinet debating the options:

> After three years of intense unpopularity [overall], they could not persuade themselves there was any wisdom in even privately discussing a serious assault on such sacred parts of the British way of life as health and public education.[105]

Because the CPRS report was so politically unpopular, Thatcher denied ever requesting or considering it.[106] When extreme measures were proposed, the intensity

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[103] Interview with Department of Energy minister.

[104] Interview with Department of Energy minister and civil servant; also see Adrian Hamilton, 'Mr. Lawson Starts the Big North Sea Sell Off,' *Times*, 20 October 1981; Lawson, *The View from No.11*, p.217; and interview with Lord Nigel Lawson, 15 February 1994.

[105] Hugo Young, *One of Us*, p.302.

[106] Keegan, *Mrs. Thatcher's Experiment*, p.193. However, Thatcher argued it was never even considered: 'The CPRS prepared its own paper...which contained a number of very radical options that had never been seriously considered by ministers or by me...I was

of middle-of-the-road opinion was raised, and proved to be a constraint to privatization. The concern over how privatization was implemented and the reaction to the CPRS report indicated that politicians were responsive to public opinion and were not free to implement an elite agenda.

With the potential for such public outcries in mind, the government sought to avoid raising any of the privatization issues outside of the region of acceptability. Responding to strong public concern for security of supply for oil, the government adapted its privatization methods accordingly. The government split BNOC and only sold the production portion, thus retaining the trading operation and the participation agreements and royalty in-kind arrangements. As a DEn civil servant pointed out, 'queues for petrol were the quickest way to lose office. BNOC gave a guarantee [of supply].'[107] On a more personal level, a civil servant related a story involving the Secretary of State for Energy, David Howell:

> There was a hiccup in supply in 1980, with the result of local shortages. Howell found this very embarrassing with a North Sea oil surplus. At the time, Howell went to fill up his car in a local garage in Wales, where the owner came over and said: "Not a very good start Mr.Howell."[108]

The civil servant thought this experience was what convinced Howell to retain the participation agreements, the thinking being the situation could have been worse without the agreements.[109]

Another measure was to create a 'golden share,' which would allow foreigners

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horrified by this paper. As soon as I saw it, I pointed out that it would almost certainly be leaked and give a totally false impression.' Thatcher, *The Downing Street Years*, pp.276-7.

[107] Interview with Treasury civil servant.

[108] Interview with Department of Energy civil servant.

[109] Interview with Department of Energy civil servant.

to buy BNOC shares, yet prevent them from gaining a controlling share.[110] As one minister explained,

> a golden share was put in to protect British interests, to prevent the takeover by a foreign power. You couldn't do this today because of European Community (EC) regulations. We were not worried about a US takeover, but rather German or French, ie through Demenex, Elf, Total or Petrofina.[111] (See discussion in Chapter Three)

From BNOC's perspective, one executive explained,

> golden shares are political measures. Even though I have worked on many privatizations since, we still don't have it right, don't know if they really do anything. At that stage [when asset sold] free market forces should work. But they [golden shares] were the vogue, the fashion.[112]

One Britoil executive complained that the golden share was a last minute response to political concerns and was not worked out, and therefore later proved to be the cause of major problems for the company as it faced takeover bids from BP and Atlantic Richfield (see Chapter Three).[113]

Another response was to re-enact the assurances agreed with oil companies in the wake of the 1974 oil crisis.[114] In July 1985, the *Financial Times* published a letter from BP to the government, assuring the government that they would meet UK demand, providing they could raise prices as necessary. The Secretary of State for Energy would only say that 'the arrangements between the government and oil

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[110] 'Government to Retain 49% of State Oil Assets,' *Times*, 21 October 1981; 'Government to Retain 49% of State Oil Assets,' *Times*, 21 October 1981, p.1; and 'No Bar to BNOC Sale,' *Times*, 3 February 1982, p.13.

[111] Interview with Department of Energy minister.

[112] Interview with BNOC executive (McCall); also see Lawson, *The View from No.11*, pp.780-82.

[113] Interview with Britoil executive.

[114] Interview with Department of Energy civil servant.

companies are confidential.'[115]

The evidence suggests that the decision to sell the oil assets was a pure political calculation, rather than one due to ideological conviction or economic efficiency goals. Civil servants reinforced the political nature of the decision: 'The government kept BNOC out of political convenience, not any conviction.'[116] Others pointed out that there was no quantitative analysis on how BNOC ensured security of supply or the impact of a sale. It was a matter of political perception.[117] In addition, the government's sales were expedient. They only sold the companies that were easy to sell, particularly those already operating as private companies, rather than those which were public monopolies or met any ideological criteria. With huge consequences for the future, civil servants also felt that the sales were undertaken without any thought to the regulatory implications.[118]

With the case of BP, by 1983 the government realized that instead of having costs concentrated in the short-term (box 9), they were in the ideal case where the majority of costs are dispersed and spread over the long-term, while the benefits are concentrated and immediate (box 11), in which case they should and did act fast. The financial distribution of costs and benefits for the BP case is illustrated in Figure 7.7. The government received almost £7 billion by 1987 in share sale proceeds while they would have had to wait until at least after 2005, 17 years later, for BP's dividend proceeds to have exceeded the sale proceeds. This is also a conservative estimate

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[115] Interview with BNOC executive; and Lawson, *The View from No.11*, pp.780-82.

[116] Interview with Department of Energy civil servant.

[117] Interviews with Department of Energy civil servants.

[118] Interviews with BNOC executive, Department of Energy civil servants; and Garner, 'British Airways and British Aerospace,' pp.22-3.

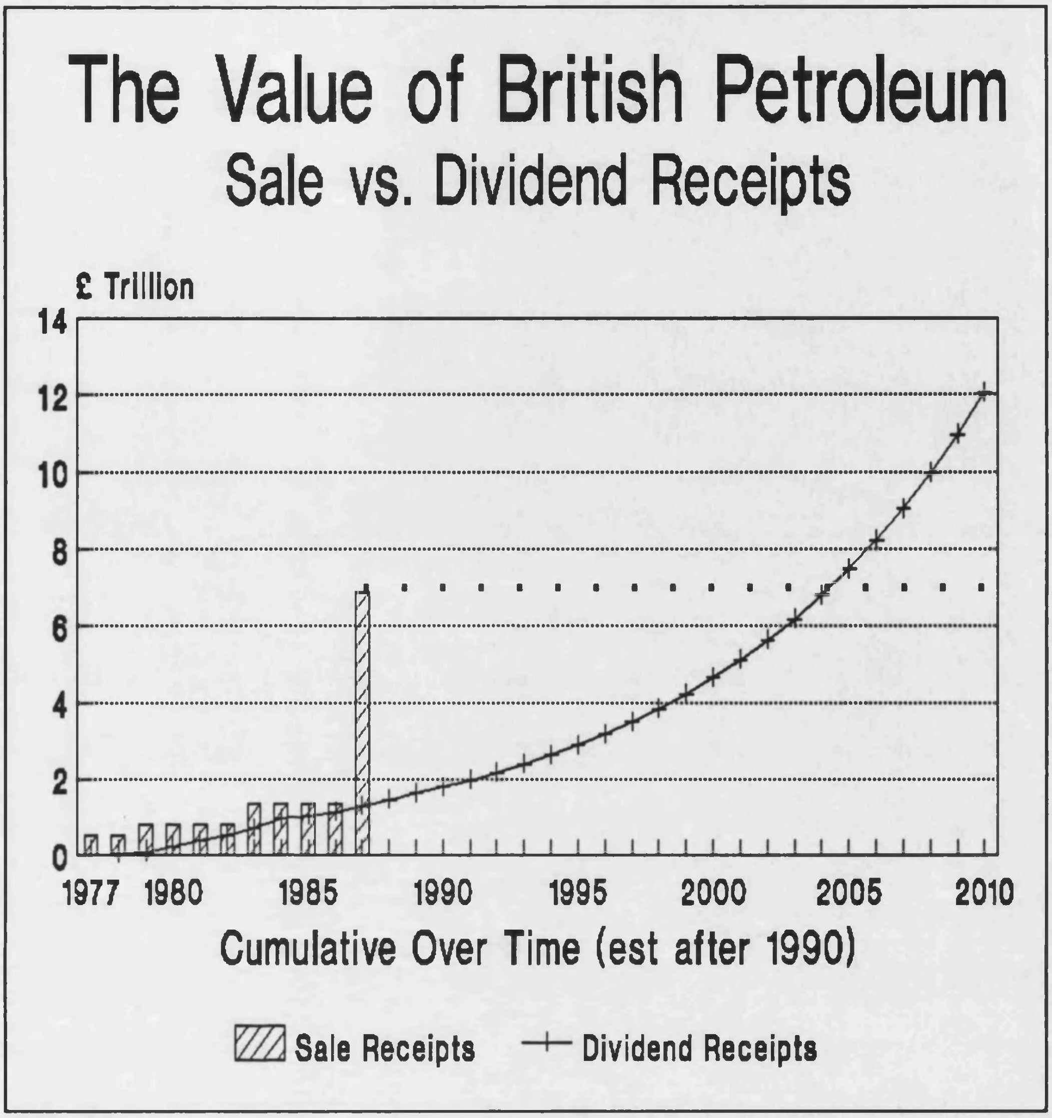

Figure 7.7.

because this graph does not take into account the net present value of money, the benefit of having cash in hand versus the promise of future revenues, which is especially important for oil companies whose dividends are not guaranteed. Thus, the costs of privatization were propelled into the future - after most of the current politicians would have retired.

The alternative explanation for the Conservative politicians' actions is that they were preference shaping, implementing policies to shape demand and increase Conservative support. Conservative politicians, in fact, claim that they shifted public opinion to favouring privatization, for example, Nigel Lawson claimed: 'Wider share ownership was an important policy objective and we were prepared to pay a price for it.'[119] For example, in the sale of Enterprise Oil, the government turned down offers of a trade sale of BGC's oil assets. They decided to float the company on the stock exchange because, according to one civil servant, the 'Conservatives had the view that capitalist shareholders would not vote for Labour.'[120] That being said, the sale was not widely advertised and no effort was made to target new shareholders.

The limit to the Conservatives' commitment to wider share ownership was demonstrated over Howell's suggestion to give all UK citizens shares in BNOC. No one in the party was prepared to support this proposition.[121] There are in fact several general advantages to 'people's capitalism' noted by academics, including; building-up a capital market, wider-share ownership, a wider constituency than a tax-cut, state-owned industries having more autonomy, relieving the state of future investment burdens, and that individuals can choose their own portfolio of risk.[122] Yet these advantages were rejected by the Conservatives, which indicates that their primary motive was the cash up front and rewards to Tory voters rather than long-term electoral gain. As one minister explained, based on his experience in the United States:

> The link in the US was that the owning class voted more conservatively. This was way underestimated by those who wanted to

[119] Lawson, *The View from No.11*, pp.237-8 and p.201; and interview with Conservative minister.

[120] Interview with Department of Energy civil servant; and Lawson, *The View from No.11*, p.757.

[121] Lawson, *The View from No.11*, p.218.

[122] Aharoni, *The Evolution and Management of State Owned Enterprises*, pp.336-7.

give it away. The link was between private share-owners and Conservative voters.[123]

The electoral impact of privatization, in terms of converting Labour to Conservative voters was not felt until the 1987 election, and then it was an estimated shift of only 1.6 per cent, controlling for the range of socioeconomic factors correlated with privatization.[124] A key reason why the Tories' policy stance converted relatively few voters was that many of the new shareholders already supported the Conservatives.[125] And while the number of shareholders in Britain dramatically increased from 5 per cent of the electorate in 1979 to 23 per cent in 1989, shareholders remained a minority of the population.[126] Even after the 1987 election, the median voter was not a shareholder. Thus, privatization might better be seen as a policy which rewarded loyal Conservative supporters rather than one which converted voters close to the median.

Determining the Conservatives' Position on Privatization

Once the costs and benefits were favourably assessed and the Conservatives adopted privatization, the position and intensity of Conservative voters' opinion on privatization determined the party's position. Rather than using the directional theory of voting which emphasizes the role of elites to determine positions and then predicts voters' response, or the median voter model which only takes into account proximity

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[123] Interview with Conservative Minister.

[124] McAllister and Studlar, 'Popular Versus Elite Views of Privatization,' p.173.

[125] Oonagh McDonald, *Owning Your Own: Social Ownership Examined* (London: Unwin Paperbacks, 1989), p.8.

[126] McAllister and Studlar, 'Popular Versus Elite Views of Privatization,' p.166; and Chapman, *Selling the Family Silver, p.8.*

of position, I suggest an alternative way of incorporating position and intensity as a means of creating demand for a policy. Adapting Figure 7.2's picture of overall voter demand for privatization, I extrapolate and incorporate additional descriptive evidence and hypothesize the distributions of position and intensity on privatization of Conservative voters (see Figure 7.8).

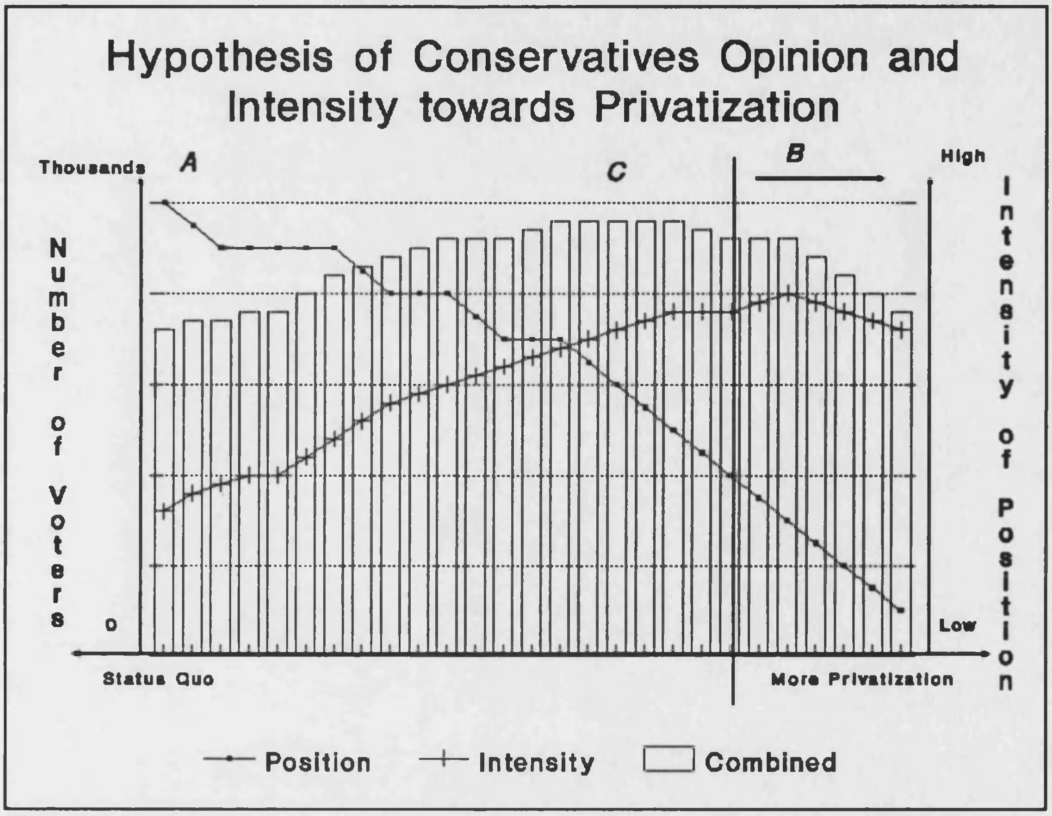

Figure 7.8.

The majority of Conservatives, like the overall population, were closest in position to the status quo, though there were many who favoured more denationalization (dotted line). In terms of intensity (crossed line), those at the neutral position did not feel strongly about the issue (point A), while those favouring more denationalization felt more strongly (point B). The intensity of those at the extreme position declined, possibly because being outside the region of acceptability (to the right of solid line) they perceived their position to be unrealistic.

Instead of parties' arbitrarily moving to an extreme position, there is an interchange between voters and candidates. Voters can influence policy positions by threatening to vote against it or by threatening to vote according to another issue, which is more likely when intensity is low. Therefore, when determining the most advantageous position to select, politicians must take into account how many voters occupy a position and how intensely they feel about the issue. By simply multiplying the position by the intensity, I determine the electoral impact of a position (bars in the background). The highest point of the bars is where the most voters will vote according to this issue. At the lower points in the bar either the intensity is less so some voters will select another issue or the intensity is stronger but there are insufficient numbers of voters to make the radical position worthwhile. Outside the region of acceptability, gains in extreme votes are cancelled out by negative votes from the center.

The Conservative party started close to the median position in 1979. As they realized the benefits from the policy, which involved the cost-benefit analysis above, and the existence of strong opinions among Conservative voters, they moved to a more extreme position (point C). A high degree of intensity from the extreme position holders led politicians further to the right. For example, Lawson records his amazement and relief at receiving a standing ovation at the 1982 Conservative party convention after changing the subject of the energy debate from rising gas prices (which were receiving heavy criticism) to the privatization of Britoil.[127]

Conclusion

[127] Lawson, *The View from No.11*, p.176.

Privatization in Britain can be divided into three phases: In the first phase, the policy was possible but was only moved along by policy entrepreneurs. In the second phase, the government was committed to the policy but only proceeded on a case by case basis according to the costs and benefits. In the third phase, privatization was accepted in general terms and evolved into an ideological project in its own right. The oil asset sales occurred during the first two phases, while most explanations of privatization focus on the third. Therefore, I argue that the traditional explanations of privatization are less helpful for this case.

The public demand for privatization was weak and uncertain over time. Opposition was greater to specific privatizations than to the concept in general over which the population was fairly evenly divided. Because privatization did not figure highly on any of the voters' rankings of issues, it did not feature in their voting decisions. It was low intensity rather than the parties' failure to offer sufficient stimulus, as the directional theory predicts, which explains the low public demand. Voters did not feel strongly about the privatization of the oil assets, in part because the policy did not affect them directly. The government, therefore, could proceed without electoral risk. This low intensity and lack of concern gave the political parties a wide range for choice in terms of developing the privatization issue and selecting their policy position.

Rather than being a 'lottery', I argue that these decisions were determined by specific supply-side factors, namely personal political advantage and party political demand. The effect of these two factors is illustrated in Figure 7.9. Personal political advantage was an important factor in both because a policy entrepreneur was important to the development and promotion of the policy. Within party political

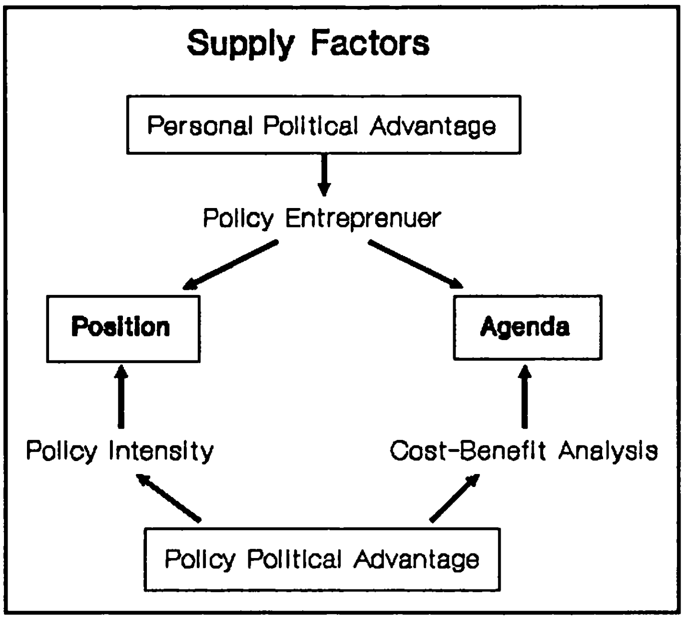

Figure 7.9.

advantage, the distribution of costs and benefits in the short and long-term determined whether privatization was worthwhile to adopt at all, while the distribution of position and intensity of Conservative party members determined the optimal position for the government to select.

In terms of policy options, the political parameters faced by the government can be illustrated in Venn diagrams where policies to raise taxes, increase the budget deficit and sell assets are represented by points A, B and C respectively (see Figures 7.10, 7.11 and 7.12). The parameters included public demand, personal credibility and electoral success as represented by circles 1, 2 and 3 respectively. In 1974, the issue of taxes and budget deficits were not intensely held issues, no politician had staked their career on them and there were no severe electoral risks for selecting any of the policies. As a result, the options available to politicians were large (points A, B and C are in all three circles), as represented in Figure 7.10. In 1977, following the 1976 balance of payments deficits and the IMF crisis, politicians could not afford to allow a repeat situation, therefore, an increase in the budget deficit due to electoral considerations was no longer possible, (point B excluded from circle 3), as illustrated in Figure 7.11. Similarly, due to the already high tax rate, Labour politicians feared they would face electoral punishment by raising taxes (point A is no longer inside circle 3). Thus, of the three options only asset sales remained possible (only point C remains in the intersection of three circles).

By 1982, the situation had changed again with the election of the Conservative government in 1979. Public opinion continued to allow politicians a wide range of options, but the Conservative leadership had staked their career credibility on their economic policy, including no new taxes while reducing the budget deficit. As such, they also faced electoral risk if they strayed from these commitments. Thus, only an asset sale was possible (point C is the only option inside circles 2 and 3 and the only option that remained in the intersection of the three circles), as illustrated in Figure 7.12.

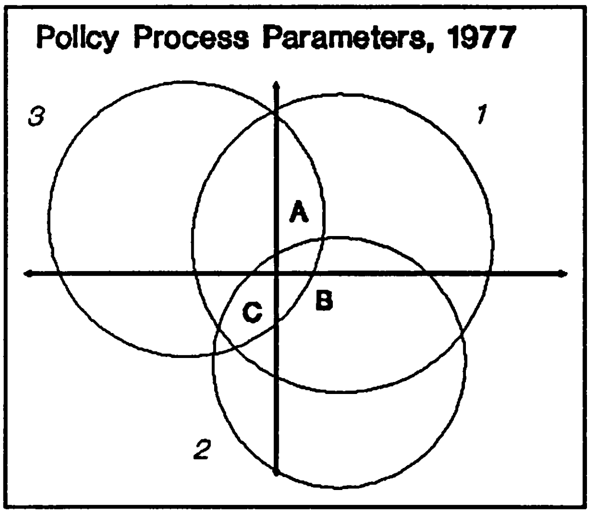

Figure 7.11.

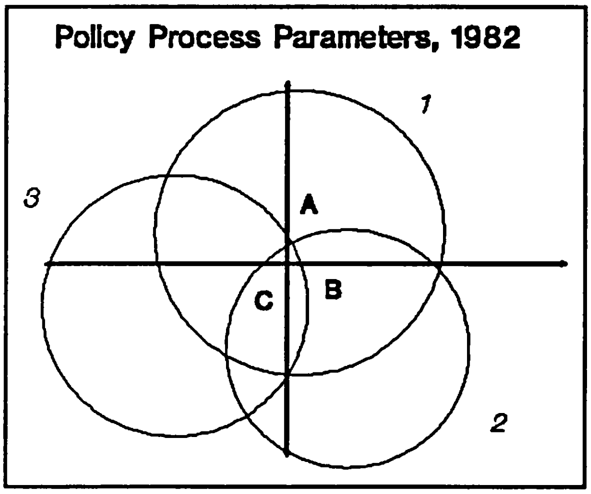

Figure 7.12.

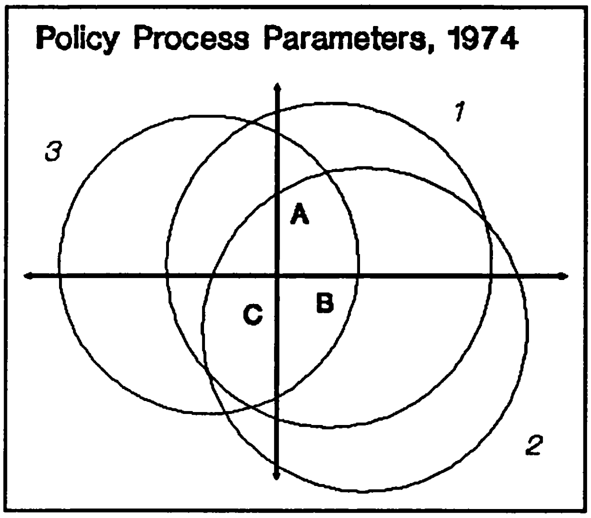

Figure 7.10.

Chapter Eight: Explaining State Disengagement

Most scholars of politics, from whatever their viewpoint, have assumed that states and governments grow larger over time, and that it is normal, logical and 'rational' for those who control government power to seek to push outward their scope of influence. Pluralists see groups, including bureaucrats, as always demanding more services and government responding by building greater capabilities to meet these demands (Dahl, 1961; Halperin, 1974). Elite theorists assume that the state is a means for elites to enhance or protect their position and thus expect elite demands to increase the scope of the states (Mills, 1956). Public choice theorists, whether focusing on the bureaucrat or the politician, have assumed that public officials have self-interested reasons for increasing the size of the government (Niskanen, 1971). Even from the perspective of international relations, scholars have accepted the realists' premise that states are power maximizers continuously seeking to increase their wealth and control, and thus their size (Keohane, 1984; Waltz, 1954 and 1979). This includes scholars from the international political economy perspective who regard states as only one of many actors in the international arena (Strange, 1985; Krasner, 1985).

Though it is not necessarily intrinsic to these theories, the government growth assumption has persisted.[1] In part, this can be understood by the fact that most governments have steadily grown, especially since World War II, the period in which most of these theories were developed. There has thus been no reason to question the growth assumption. In fact, government growth seemed to be the one constant that

[1] Hood, 'Stabilization and Cutbacks,'p.43-5.

political theory had to be able to explain. The idea and practice of 'rolling back the frontiers of the state' which developed in Britain under the Thatcher government, and the effort to disengage government from many spheres of economic and social life, initially raised few doubts about the fundamental premise. A common first response was to be sceptical about whether anything had really changed.

But the longer and more complete a process of state disengagement becomes, the less plausible it is to suppose that nothing of substance has happened, and the more important it becomes to examine the possibility that public officials, groups, elites or states have acted to reduce state power or influence in a long-term way, and therefore have in some sense behaved counter-intuitively. The British government's oil asset sales apparently provide just such a case. They stretched over a ten year period, involved 9 separate sales, and affected assets valued by the private market at £8.5 billion. The sales were a particularly final and once-for-all method of readjusting government's role in the energy sector: the scale of receipts made it virtually impossible for any future government to rebuild any equivalent asset portfolio without changing the whole basis of government/market relations in the UK. The sales were also a serious undertaking in terms of their transaction costs, conservatively estimated at some £223 million.

Because the underlying assumptions of most theorists are inconsistent with these facts, it is important to stand back somewhat from the theories and the detailed narratives reviewed so far, and briefly re-piece the jigsaw of multiple causes involved. Table 8.1 summarizes the general motivations for selling an asset, which can be divided into two categories: financial and functional. Though this list is derived from governments selling state assets, perhaps it can more readily be understood using the analogy of a professor with a ten year old automobile.

Table 8.1. Why Sell an Asset?

Financial	Functional
Expensive to maintain	Asset changed in terms of: size capabilities output and therefore no longer provides necessary service
Becomes a financial liability	
Need the money	Needs change in terms of: political ideological social and therefore asset no longer necessary
Other arrangements offer greater returns	Better alternatives available

While there are many reasons why the professor might reconsider ownership of a ten year old car, there are only a few specific reasons why she should actually sell it. Initially, financial reasons might motivate a sale. For instance, the car is expensive to maintain because it breaks down so often, or it has become a financial liability as the make and age of the car increase the likelihood of accidents which have repercussions in the form of an enormous insurance liability. In other scenarios, she needs money for more important priorities, such as to pay her landlord who has been knocking on her door for the last week, or she has realized that leasing a car is more economical. In addition to financial motivations, there are also functional reasons why a professor might sell her car: Either the asset has changed so that it no longer provides the same service, or her needs have changed and she no longer needs the same service or a better alternative now exists. For example, the car has become so run-down it is no longer the reliable mode of transportation it once was, or the professor has grown out of her idealist beliefs and a ten year old Russian Lada does not fit with her new conservative image. A final possibility is that the public transport link from her home to university has recently been completed and the 45 minute drive can now be done in 20 minutes on the underground. Of course, she will act faster to dispose of the car the more she needs the money or the more embarrassing it is to have a Lada parked in her driveway.

Given these numerous 'rational' reasons to sell an asset in general, I now turn to the evidence of this case and review which rationales applied to the sales of BP, BNOC and BGC's oil assets from the perspective of the four levels of influences analyzed in this paper: International, company, bureaucracy, and political process. I first examine the international level and consider the theoretical implications for using this level for domestic policy decisions. Then I turn to the domestic actors, the managers of BNOC, BGC and BP, the civil servants and then the elected politicians and review their role in the asset sale decision. In the third section, I consider some broader implications of this analysis, first for understanding or predicting the extent of privatization in other contexts, and second for improving the efficiency of government bureaucracies. I then conclude by returning to an overview of this case and the implications of a multi-level approach.

8.1. International Factors in State Disengagement

At the international level I argued, in contrast to the realists, that rather than determining a state's behaviour, international factors set parameters to politicians' policy choices. With two variables, an aggregate political variable and an economic issue specific variable, it is possible to predict a country's vulnerability to international pressures in different cases. In Britain's case, it was clear that the British government would be more susceptible to international financial pressures than international oil pressures. In fact, pressures on Britain's finances in the form of the 1976 IMF crisis were the only international forces that directly affected the government's decision to sell its oil assets. Changes in the structure of the international oil industry from a cartel to a free-market industry did not force the sales in the late 1970s or the 1980s, but they were significant in that they diminished the consequences of relinquishing ownership and this made the sales possible. In response to neo-liberal claims, the third variable examined in this case was Britain's membership in the EC and the IEA. The evidence revealed that the international organizations per se had little effect on the government's decision to sell its oil assets. The interdependence that led to the creation of the organizations, however, was an important factor. The economic links can be revealed through issue analysis, rather than specific organizational studies, as was the case with the IMF in the financial issue analysis.

Recalling Table 8.1, the international level was the primary determinant of the government's functional motivations for selling its oil assets. In the case of Britoil, Enterprise Oil and Wytch Farm and BP, and even in the case of winding down BNOC's trading operation, the changes in the structure of the international oil industry were such that the services that the oil assets provided were no longer needed in Britain. Specifically on the demand side, as the global oil industry became increasingly controlled by the free-market, numerous sources of oil were developed and state-ownership was no longer necessary to ensure security of supply. On the supply side, the changes were such that BNOC trading and BP were no longer able to provide the services they once did. Due to the extent of free-market competition, a single state could not influence oil prices through a state trading company, especially a relatively small company like BNOC and with Britain's relatively modest reserves. Similarly, though BP could once be relied upon to favour Britain, as the company sought to adapt to the changing international structure, it was no longer possible for BP to discriminate between customers.

The approach used in this case contributes to general knowledge of the role international factors play in policy-making analysis, but it also contributes to understanding of the theoretical underpinnings of international relations theory. This case suggests that international factors can be incorporated as setting parameters in the same way that institutional public choice theorists have considered domestic institutions. While this seems especially obvious in cases of privatization, which is often referred to as part of an international trend, international factors are also useful in general to domestic policy-making analyses. This case, in fact, helps to illustrate how few truly 'domestic' issues there are, especially for states in weaker international political and economic positions.

In terms of broader international relations theory, the British oil asset sales question one of the basic assumptions regarding the state. International relations has evolved beyond realism to neo-realism and neo-liberalism, as well as other avenues such as international political economy (IPE). But in the two mainstream areas, neo-realism and neo-liberalism, the central assumptions have remained - the state is the primary actor, the international system is basically anarchic and states seek power. This case, with many others in the IPE genre, shows that there are important issues which a state-centred approach cannot adequately address.

The most fundamental criticism of the neo-realist approach is that they treat the state's preferences as a given. They assume that the agents and actors of the state are unitary, only the state's capabilities affect the system, and that international institutions play a minimal role (Krasner, 1985). Neo-liberals only challenge the latter two problems and argue that factors such as interdependence and institutionalization of international rules (international organizations or regimes) are also important. Indirectly they question the pre-eminence of the state, but they do not deny that it is an important international actor.[2] Only IPE scholars have pointed out that there are other actors such as firms and groups and other constructs such as markets that matter.[3] Some also highlight the complexity of the state and show that it is not a homogenous actor but rather a compilation of political parties, interest groups, politicians and voters.[4] This re-definition of the state cannot be understated; its significance has far-reaching implications.

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[2] Krasner, *International Regimes*.

[3] Strange, *States and Markets*; and Keohane and Nye, *Power and Interdependence*.

[4] Milner, *Resisting Protectionism*; Cohen, 'European Financial Integration and National Banking Interests'; Frieden, 'Invested Interests'; and Golich, 'From Competition to Collaboration.'

By focusing on the state as a homogeneous, rational actor, we miss out on other actors and explanations. For example, states with different parties in power will have the same capabilities and face the same international parameters, and therefore have many of the same policy choices. But where there is room for choice, outcomes may be different because politicians have different constituents, different party structures and different political strategies. These factors affect their policy choices, which in turn affect the state's resources. In the British case, the change of the party in power - and the ensuing interests and strategy changes - resulted in the complete sale of the state's oil assets and a re-definition of the state's position.

The effect of changing this one assumption is also evident from the difference between the findings in this study and those of Merrie Gilbert Klapp, who accepts the statist's assumptions, including that states have definable interests unique from society.[5] The first difference is over what determines the desirability of state ownership. She argues that governments become involved or not in the oil business due to changes in the role of the state, that is, because of a change in the state's position vis-a-vis private domestic and foreign interests (p.130-1), whereas I argue that governments become involved or not in the oil business due to changes in the international oil industry, from a cartel to a free market, as well as other domestic factors. Whether a state becomes stronger or weaker versus domestic and international interests does not seem to explain why states at very different stages of development became involved in the oil industry during the past 70 years. The changes in the international structure of the oil industry better explain the ownership trend. When the oil industry was a cartel, there were monopoly rents to be gained

[5] Klapp, *The Sovereign Entrepreneur*, p.38.

through ownership and loss of security if ownership was not possible. Thus, in the face of the majors' monopoly and OPEC's cartel, state ownership of companies continually increased. However, once the industry structure shifted to a free-market, the gains from ownership were not as great nor were the security costs of foregoing ownership - and the privatizations began.

The second difference is over causes of state ownership. Klapp argues that: 'The ownership of industry will depend, in the long run, not on ideological preferences but on struggles for wealth between great organizations - states, multinational corporations, and domestic companies.'(p.15) While she admits that states have internal disputes, she argues that they maintain distinct national interests. By contrast, I argue that states are not homogenous and that politicians, not states, seek advantage and power. Similarly, MNCs and domestic companies are not homogeneous blocks. The struggle for power, however, is not limited to these groups; politicians, consumers, taxpayers, voters, oil competitors and environmentalists are all political actors able to influence outcomes. The policy outcomes depend on who is in the winning coalition, as well as other parameters such as the bureaucracy and voters. Establishing the relative strength between Klapp's three groups does not have the same predictive power.

Finally, and not surprisingly, our predictions also differ. Klapp predicts that: 'the current still runs in the direction of state entrepreneurs and that privatization, at least as far as oil is concerned, is no more than a diversion.'(p.15) By contrast, I argue that privatization is perfectly sustainable as long as the free-market in oil remains. Klapp assumes that all states have an autonomous interest in the ownership of oil (p.131), but outlines no underlying logic showing that this should be so. I argue that better predictions can be made by examining the situation from the opportunities offered by the international system, such as a monopoly or free-market oil industry, as well as the domestic demands of consumers and voters. In this way we can gain a better understanding of why governments chose ownership of oil companies in some cases and regulation in others. In fact, control over industries can be ensured through numerous means including: competition policy, regulatory policy, regional policy, employment and training policy, industrial relations policy, policy for high technology industries, trade policy, public procurement policy, planning and environmental policy, energy policy, and corporate tax policy.[6] Klapp's broad predictions do not seem to accept that these alternatives to ownership are sufficient; whereas I argue that in many cases they are, in fact, politically preferable.

Governments' reactions to foreign ownership provide an interesting and specific test for these two approaches. Foreign ownership of major assets is a sensitive issue in any country and highlights exactly how the national government evaluates the benefits of domestic control. As an industrialized country with a well developed international financial market and a sizable number of domestic investors, Britain did not face the same financial constraints as many less developed countries. Even so, the domestic British market was not large enough to completely absorb the BP share offerings in 1977, 1983 or 1987, so tranches of each offering were placed overseas. The issue of foreign ownership was not controversial, however, until the 1987 stock market crash when the Kuwait Investment Office (KIO) acquired over 20 per cent of BP's total shares. Until then, foreign investors were most likely to be

[6] Vickers and Wright, 'The Politics of Industrial Privatisation in Western Europe,' pp.26-7.

from other industrialized countries with similar beliefs in the free-market system. No matter who held the shares, the market mechanism would function, providing efficient allocation of oil. When the KIO began to seek a controlling interest in BP, however, the government realized that, as the arm of an oil producing country, KIO might seek monopoly advantages. A BP controlled by KIO might also fail to respond to Britain's oil demands. The subsequent actions of the British government might support Klapp's claim that relinquishing ownership is a blip in history. If the British government had irrevocably decided not to own its oil assets, why should the Kuwaiti government, through the KIO, not take advantage of the opportunity to expand its own oil assets?

The Thatcher government, however, did not re-purchase the shares. Contrary to their free-market policy stance, they intervened using other instruments, forcing the KIO to divest from BP. These actions can be best explained as nationally-elected politicians responding to public demand. The public outcry and the perceived short-term costs of hostile interests controlling one of Britain's major oil suppliers caused significant public demand for a government response. Klapp's argument suggests that even a 'weak' state would re-gain ownership, but the government used alternative tools available to ensure BP's independent status. KIO was not the only example of the British government intervening to protect the interests of its former assets. The government also prevented the British mining conglomerate RTZ from taking over Enterprise Oil in 1984, and prevented a U.S. oil company take-over of BNOC in 1988, though it allowed BP to do so subsequently. Realists, by insisting on seeing the state as a unitary actor with distinct interests, blur our view of the real motivations and actors in policy-making.

8.2. The Domestic Actors' Calculus

This section reviews the motives of the domestic actors involved in the decision-making process, and then examines which factors were included in the calculus for each sale.

The Three Main Actors

At the **Company** level, by examining the level of organizational autonomy, financial independence, and success in achieving the company's mission, it was possible to explain the differing actions of BP, BNOC and BGC. Because BP was organizationally autonomous and financially independent, it sought to maintain that status. Due to its considerable size and financial success, BP was effective in persuading the government to sell its holding. By contrast, BNOC and BGC depended on government ownership for their national interest mandate, which they resented losing. But as autonomous and independent companies, they also resisted any measure that would split their companies. Due to its enormous size and financial success, BGC was effective in delaying the sale of Wytch Farm for over two years, but ultimately could not stop either of its oil assets being sold. BNOC was the least successful in defending its interests as the government was able to appoint a new company chairman favourable to privatization.

Opposition from the managers of nationalized industries can most easily be avoided by replacing the top executive with a manager who does not have any allegiance to the company and is favourable to the government's change in policy. If that is not possible, or if opposition continues, the most effective means to appease concern and gain cooperation is to sell the company in one piece. Though this may undermine attempts to increase competition and efficiency in the case of monopolies, it will normally increase the value of the company as well as the proceeds to the government. Because a government's time horizon is only the next election, measures that facilitate a sale so that it is achievable during the party's time in office are most desirable, and the consequences of a private monopoly will immediately be no different than a public monopoly. Only in the long-term will disregard for the public interest become apparent, and measures can be implemented subsequently to break the monopoly.

At the **Bureaucracy** level, British civil servants were motivated by interesting work that was defined in part by the career opportunities that privatization presented. One traditional public choice view of bureaucrats is that they are budget-maximizers. Depending on whether there is movement within the bureaucracy and whether bureaucrats choose to act individually or collectively, though, three other types of action are possible: self-maximizing, bureau-shaping and career-maximizing. This traditional view is especially misguided because collective action is rare. In this case, because British civil servants moved between divisions and departments regularly, their allegiance was to the central government rather than to a particular department or division. Thus, their interests focused on interesting work and career advancement rather than defending the functions of their current division or department.

A strong/weak department - personal affect typology explains why collective action was possible in strong departments where policies were perceived negatively; otherwise individual strategies were more rational. Because the structure of the British civil service was so secure, very few policies were interpreted by civil servants as personally negative. Collective action, therefore, would have been unusual. And because the Department of Energy was a relatively weak department, the lack of collective action in this case is not surprising. However, the fact that collective action was evident in the Treasury suggests that civil servants do react when they perceive a policy shift that threatens them personally and that they are capable of doing so. It also suggests that there are more ways to react in a stronger department; no other department, for example, could realistically promote sales of other departments' assets.

At the **Political Process** level, traditional public choice models, such as the median voter model, focus on the demand for policies and predict that politicians will select policy positions that appeal to the largest number of voters. This case lends support to the view that, for some issues, there is no strong demand and policy decisions are made primarily according to supply factors. In the case of privatization in Britain there was little demand in the early stages of policy development. The deciding factors were, therefore, from the supply-side: personal political advantage and electoral political advantage. Privatization provided the ideal electoral advantage where benefits were concentrated towards Conservative supporters in the short-term and costs were dispersed in the long-term. Originally the Conservative leadership hesitated about selling oil assets, fearing they were in the disadvantageous position of threatening concentrated short-term costs to supporters and opponents alike. But a policy entrepreneur emerged to push the policy through the early stages of internal resistance and emphasized that there would be no short-term costs from the sales, that ownership of oil assets would not change Britain's oil situation, even in a crisis, and that the proceeds from the sale would provide immediate cash to distribute to supporters. Once they accepted this distribution of costs and benefits in the short and long-term, the Conservative leadership proceeded quickly.

When looking at the three sets of domestic actors, company managers, civil servants and politicians, their reactions towards privatization were quite different. The managers of BNOC and BGC were opposed while the managers of BP were enthusiastic. The civil servants in the DEn were initially sceptical but were cooperative while those in the Treasury were eager. Among the politicians, most were initially reluctant while a few policy entrepreneurs were enthusiastic. These variations can be explained by the differences in the actors' constraints, but also by their goals and motivations. The importance of looking closely at constraints is illustrated by the variations just between the managers of BP and BNOC. Both were state-owned oil companies and yet their reactions to privatization were completely different. Thus, even slight variation in structure can produce widely different outcomes. This also highlights the problem of assuming bureaucratic structures to be similar, not only between countries, but within them - as many public choice theorists do.

Despite the differences, calling attention to the constraints reveals new sets of generalizations about actors: They seek to maximize their utility in the short-term, and their strategies are influenced by both the constraints of the institutions in which they function and by their own capabilities. In other words, neither constraints nor individuals are generic. Individuals pursue goals as they become possible within the existing structures, and as they are able. For example, a civil servant in a flexible bureaucracy who is not an effective manager may choose to stay in their current bureau or department and not seek promotion. As a result of this choice, the civil servant will then pursue self-maximizing strategies in that department. Without knowing the structure of the bureaucracy and the individual's abilities, it is difficult to predict such behaviour. Only upon careful examination of actors and their particular constraints can we understand their actions.

The Calculus

In deciding to sell the oil holdings, all three sets of actors as public officials can technically be described as decision-makers. But in this case, only the politicians were able to make the final decisions to sell assets, albeit under the influence not only of the company managers and civil servants, but also of public demand as well as international pressures. The influences and thus the explanation for each privatization differ.

The numerous political reasons for selling each oil asset are summarized in Table 8.2. The reasons were surprisingly similar, though the priorities in each case differed according to the company and other external pressures. For the oil assets sales, the financial motivations were pre-eminent. The need for money was of primary importance to the government and the attractiveness of a sale was enhanced because the politicians could raise large amounts of money immediately. According to political short-term calculations, this was a more advantageous financial arrangement than the returns in the form of profits and dividends spread over the longer term. In the case of BNOC's trading operations, while there was no option to sell the organization, the financial liabilities that it represented were the trigger to motivate politicians to close it down.

Table 8.2. Political Motivations for Selling Oil Assets				
	Britoil	BGC'S Oil Assets	BP	BNOC Trading
Party Political	Financial need Other arrangements offer greater returns Ideological inconsistent	Financial need Other arrangements offer greater returns Ideologically inconsistent	Financial need Other arrangements offer greater returns Expensive to maintain	Financial liability Ideologically inconsistent
Personally Political	Inconsistent with image Prestige from sale	Inconsistent with image Prestige from sale	Inconsistent with image Prestige from sale	Inconsistent with image

Functional motivations were also important. In the case of BNOC and BGC, the Conservatives' needs had changed so that state-ownership was no longer consistent with their free-market ideology nor their image as champions of the private sector and small government. There was also a better alternative available than state ownership, namely private ownership and the ensuing prestige from the sale and from governing over a larger private sector.

Though the factors in each case were similar, the priorities differed. In the case of Britoil, the personal prestige factor for Nigel Lawson was the most important factor, followed by the fact that a sale offered an immediate cash return whereas continued ownership meant variable profits into the future. Of underlying importance was the government's need for money, as well as the way it fit with the Conservative's free-market ideology and the Conservative leadership's image as defenders of the private sector.

In the case of BGC's oil assets, the most important factor was the improved financial arrangement that privatization offered. It was superior in terms of immediate cash up front, and because the sales also reduced the strength of the remaining BGC, an important objective for the government, which had been frustrated in its struggle to control BGC's profits. The political prestige from the sales was also important, though not realized in the Wytch Farm case because of the long duration of the sale. As in the Britoil case, the need for money and the inconsistency in both ideology and image were important as secondary factors.

The BP case is more complicated because there were several sales, though they can be divided between the Labour's 1977 sale and the subsequent sales by the Conservatives. For the 1977 sale, the most important factor was the need for money and the fact that the sale would raise immediate cash without lessening the government's control over the company. Raising money in this way was more consistent with Labour's image than cutting spending. The maintenance expenses and the prestige, however, were not factors in 1977. For the Conservative's sales, in contrast, the prestige was of primary importance, as were the enormous proceeds up front. The expense of maintaining a stake in BP was also important. Though the image of having companies under state-ownership was a factor for the Conservatives, ideological consistency was not an issue as it was in the other cases because BP was not subjected to government intervention and was already functioning efficiently in the private sector.

Finally, the case of the BNOC trading operations offers a slightly different perspective. Though the trading operation did not fit with the Conservatives' free-trade ideology nor with their image of themselves as efficient managers, there were overriding factors that made the operation worthwhile to maintain, such as national security. But as the company began to lose money, which in turn had to be covered by grants made expressly by Parliament, it highlighted the incompatibility of BNOC with the government and hastened its demise.

8.3. Broader Ramifications

While the findings are understandable for this case, the real test is whether they can be applied to cases beyond privatization in Britain. Extrapolating from the findings, I create a list of probing questions to reveal whether these factors exist in other countries and therefore whether privatization is likely. It might be objected, however, that privatization is an unusual governmental policy. To investigate whether the more general findings of this case have broader applications than just privatization, I apply them to a current discussion on 'reinventing government.' From these two explorations, I reconsider the overall findings of this case and the usefulness of this approach.

Empirical Implications for Other Privatizations

If adding the pieces together to explain privatization is a truly viable approach, it should be able to identify general conditions under which privatization is likely to occur.[7] A series of general questions can be asked of any country which can

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[7] Savas, *Privatization*, p.278-9.

determine whether and when privatization is a realistic policy outcome (see Table 8.3). I apply the questions to the specific case of Argentina's energy privatizations, and then to perceptions of an international privatization trend.

Table 8.3. Anticipating Privatization	
1.	Does the country have assets that can be sold?
2.	Due to international or political pressures, does the government need money quickly?
3.	Will the company managers cooperate, and if not, does the government have means to circumvent them?
4.	Will the bureaucrats in the relevant departments cooperate, and if not, does the government have the means to circumvent them?
5.	Can the governing party implement the sale without electoral punishment, i.e. is public opinion opposed and intense on the issue?
6.	Are there other options that will provide greater political advantage for the politicians in power?

My findings in the British case of privatization of oil assets revealed that there were many layers of obstacles to privatization. The questions in Table 8.3. are designed to reveal whether obstacles exist in other cases. While not designed to discover the intricacies that contributed to our understanding of the British case, these questions may be useful in obtaining a first approximation assessment.

A 'no' to any one of these six questions can prevent privatization from occurring. The first pre-condition for a sale is whether there is anything to sell. In some countries the government never created or nationalized industries, therefore there is little to sell. In other countries where financial markets are small and undeveloped, having something to sell means having assets that are attractive to international investors. The second question determines whether there is a pressing need for money. If time is not crucial, there may be other more feasible options. Question 3 focuses on the managers of the state-owned industries. Privatization can proceed only if they cooperate or the government has the means to override or replace them. Question 4 addresses a similar consideration in regard to the government's civil servants; privatization can only proceed if they co-operate or the government has the means to circumvent or replace them. Question 5 considers the electoral implications of a sale. If the public is opposed on the grounds of national interest, strategic security, financial or even sentiment and votes accordingly, privatization is not worthwhile for a politician to pursue and the policy will halt. Finally, if politicians have other options which provide greater personal or party political advantage, they will be selected instead of privatization. Over time, questions 3 through 5 may be altered by political means, which is part of the job of a political entrepreneur. The other questions depend on structural factors and alternative options which for the most part are external to the political process.

To explore the usefulness of these questions beyond the case of Britain, I apply them to the case of Argentina, one of the few cases where a government has decisively moved on and successfully completed an extensive privatization programme, including its energy assets. In fact, it is the only government besides Britain to completely dispose of its oil assets.[8] Argentina's energy assets include Hidronor, the country's principal hydro-electricity generator, YPF, the national oil company, and the federally held gas and electricity companies. Equally remarkable is the fact that these energy assets were sold in 15 months, from March 1992 to July 1993 and raised $6.65 billion.[9]

The Argentinean case passes the six hurdles for privatization: The answer to question 1 is that as a developing country, Argentina's energy industry was one of the few state-owned resources that would sell. Because the government of Argentina in 1990 was facing 200 per cent inflation and a fiscal deficit of 22 per cent of GDP, the answer to question 2 is that they needed money quickly, particularly foreign exchange, in order to repay their international debt and to stabilize their shaky economy.[10] With a small indigenous investment market, Argentina could only sell assets that were attractive to international investors. On question 3, the Argentinean government demanded safeguards including investment and other requirements from the investors, so that ministers argued that they were able to ensure Argentina's energy security. On question 4, the government was able to overcome management opposition to privatization by hiring an oil industry veteran from the private sector expressly to oversee the privatization of YPF.[11] In relation to question 5, President

[8] There are, however, a few countries whose governments never owned their oil assets, such as the United States.

[9] John Barham, 'International Company News: Argentina Sells Energy Group in Three Units,' *Financial Times*, 12 July 1993, p.19.

[10] David Mulfor, 'Argentina Privatizes Oil and Vitalizes Stock Market,' *Wall Street Journal*, 12 November 1994, p.A15.

[11] Mulfor, 'Argentina Privatises Oil and Vitalizes Stock Market,' p.A15.

Carlos Menem, with the powers of the Presidency behind him, was able to overcome any opposition from government bureaucrats.[12]

On question 6, the government was able to avoid electoral punishment by convincing the public in two distinct ways that the sales were economically essential. First, the government bought the support of the politically important old age pensioners by allocating a substantial portion of the share offerings to them in order to make good billions of dollars in unpaid bills. There may be electoral repercussions in the future, however, because 30-35 per cent of the shares were subsequently purchased in the market by foreign investors.[13] Second, the government argued that the sales were crucial to the country's economy. Privatization ended \$2.1 billion annual subsidies to nationalized companies; generated additional taxes from some companies now operating profitably in the private sector; transferred \$1.5 billion in liabilities to the private sector; added \$5.4 billion in cash to the Treasury, and enabled them to retire \$12.5 billion in government debt through equity swaps.[14] Because the Argentinean Constitution allows Presidents to serve only one term in office, Menem did not have electoral considerations to weigh, and thus he could pursue the policy without repercussions. He is, however, now making moves to alter the Constitution to allow himself another term. Answering the last question, number 6, in terms of personal political advantage, Menem has been widely credited with stabilizing the economy. This achievement cannot hurt his future career aspirations

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[12] David Battman, 'Survey of Oil and Gas Industry: Liberalisation Pay Off,' *Financial Times*, 13 December 1993, p.33.

[13] John Barham and Damian Fraser, 'International Company News: Argentina Pins Hopes on YPF Offer,' *Financial Times*, 25 June 1993, p.25; and Mulfor, 'Argentina Privatizes Oil and Vitalizes Stock Market,' p.A15.

[14] Stephen Fidler, 'Survey of Argentina,' *Financial Times*, 27 May 1993, p.36.

and may be the impetus needed to alter the Constitution and grant him another term in office.[15]

Looking beyond the case of Argentina, despite the *Economist*'s claim that 'Everybody's doing it,' privatization has in fact been a limited phenomenon. Many states have considered sales and other means to reduce the size of their government. And many leaders have proposed such actions, but few have been implemented. Given the multiple and complex conditions affecting the privatization decision, as represented by the hurdles in Table 8.3, it is surprising that so many governments have chosen privatization at all and have been able to implement their privatization plans.

A review of the countries mentioned in Chapter One as part of the privatization phenomenon shows that very few have actually completed major sales. For example, Turkey has raised $1.7 billion primarily through sales of minority stakes, often in companies already in the private sector.[16] Pakistan was scolded by its international donors over the lack of progress on its privatization programme, which was only begun in 1991 with small disposals and the sale of 51 per cent of a large company, National Fibres Ltd.[17] Belgium privatized its first asset in October 1993, a network of insurance and banking branches; even then the government sold only 49.9 per cent of the company.[18] Spain has just slowly started to sell state

[15] Fidler, 'Survey of Argentina,' p.36.

[16] Anne Counsell, 'Survey of Turkey,' *Financial Times*, 15 April 1994, p.V.

[17] Farhan Bokhari, 'Survey of Pakistan,' *Financial Times*, 18 September 1992, p.IV; and Farhan Bokhari, 'Pakistan to Ask Donors for Pounds 1.7bn,' *Financial Times*, 23 February 1994, p.4.

[18] Andrew Hill, 'Survey of Belgium Banking and Finance,' *Financial Times*, 25 November 1993, p.IV.

assets, such as 13 per cent of Repsol, the energy group, and 25 per cent of the state-owned banking corporation.[19] In Mexico by 1992, the government sold the 18 banks which were nationalized in 1982, which raised the substantial sum of $12.4 billion.[20] The Mexican government, however, has not touched the more traditional state-owned industries. For example, President Carlos Salinas at Pemex's recent 54th anniversary stated: 'The property of oil stays uniquely and firmly under the control of the Mexican state.'[21]

Even those countries heralded as exceptional cases still maintain state ownership. Malaysia, for example has been highlighted by the *Financial Times*:

> Where others have talked, Malaysia has acted. For the last decade, the government has embraced privatization with an enthusiasm rarely matched elsewhere.[22]

Over the last ten years, the sales have targeted 54 organizations. But of the major government corporations, only portions have been privatized, such as 23 per cent of Tenaga Nasional (the state electricity utility) and 30 per cent of the Malaysian-based Mitsubishi-type Proton cars.[23] Similarly, Hungary has been touted as the most successful Eastern European country in implementing privatization, as the government has sold 15-20 per cent of the state's holdings. But their programme has now come

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[19] Tom Burns, 'Survey of Spain, Banking and Finance,' *Financial Times*, 23 June 1993, p.V.

[20] Fidler, 'Survey of Mexico,' p.III.

[21] Damian Fraser, 'World Trade News: Mexico Faces Hard Choice in Keeping Oil Out of NAFTA,' *Financial Times*, 11 June 1992, p.3.

[22] Victor Mallet, 'Survey of Malaysia,' *Financial Times*, 28 August 1992, p.VI.

[23] Mallet, 'Survey of Malaysia,' p.VI.

to a standstill with the state still holding a substantial portion of industry.[24]

Most countries cite the need for obtaining money quickly as a reason for privatization. In Turkey, Belgium and Spain, the need to curb growing budget deficits and restore policy credibility were key trigger factors.[25] Many cash-starved governments, of course, do not have the other conditions necessary to privatize. This evidence supports my contention that an obstacle to any of the six conditions is sufficient to prevent privatization. The most common obstacle comes from the electoral unpopularity of government withdrawal (question 6). In India, Turkey, Hungary, Argentina, Columbia, Peru, Venezuela, Nigeria and Ghana, the threat of electoral punishment was mentioned as a serious obstacle to privatization. Thus opposition is often in forms more extreme than those found in Britain, including terrorism, coups, and threats from powerful opposition parties to re-nationalize any assets - factors which have the double effect of also discouraging investors.[26] Of course more in-depth analyses are needed to reveal the reasons why these obstacles exist and how they might be overcome. But these 6 questions appear to be a useful guide in identifying the sources of obstacles to privatization across countries.

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[24] Nick Clegg, 'Hungary's Privatisation Falters After Flying Start,' *Financial Times*, 19 October 1993, p.4.

[25] John Murray Brown, 'Turkey Plans Big State Sell-Off,' *Financial Times*, 11 February 1993, p.3; Hill, 'Survey of Belgium Banking and Finance,' p.IV; and Burns, 'Survey of Spain, Banking and Finance,' p.V.

[26] Nick Clegg, 'Hungary's Privatisation Falters After Flying Start,' *Financial Times*, 19 October 1993, p.4; John Murray Brown, 'Turkey Plans Big State Sell-Off,' *Financial Times*, 11 February 1993, p.3; Tony Hawkins, 'Survey of Africa,' *Financial Times*, 1 September 1993, p.XI; Kunal Bose, 'Survey of India,' *Financial Times*, 30 September 1993, p.XI; and Sheila Jones, 'Survey of Turkish Finance and Industry,' *Financial Times*, 25 November 1993, p.V.

Considerations for Optimal Government

Scholars have been concerned with the design of an optimal political structure for thousands of years, and the search continues.[27] As a means to broaden the findings in this case of privatization, I consider the results with reference to a currently influential book on changing bureaucracy in the United States, *Reinventing Government* by David Osborne and Ted Gaebler, which is now being read and discussed by politicians and civil servants in Britain.[28] The evidence from this case suggests that the changes being proposed by Osborne and Gaebler may be more complex than they imply. As this case study shows, even slight differences in institutional structure, motivations or actors' assessment of change can cause a wide range of outcomes. In a recent interview, David Osborne emphasized that the changes rest on carefully defining bureaucracies' business, mission, and customers.[29] Evidence from this case supports their contention, but also reveals how difficult an accurate definition is to create. A generalized approach may negate the intended effect.

The example Osborne and Gaebler herald as a success illustrates my point. A unit within the U.S. Department of Defence in charge of all defence installations has simplified its charter to a one page sheet that defined their business, mission and customers: 'To provide for our customers - the soldiers, sailors, marines, and airmen

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[27] Richard Auster and Morris Silver, *The State as a Firm: Economic Forces in Political Development* (London: Martinus Nijhoff, 1979), p.1.

[28] David Osborne and Ted Gaebler, *Reinventing Government: How the Entrepreneurial Spirit is Transforming the Public Sector* (New York: Addition-Wesley, 1992).

[29] Todd Carver and Albert Vondra, 'Reinventing the Business of Government: An Interview with David Osborne,' *Harvard Business Review*, May-June 1994, p.133.

who defend America - excellent places to work and live, and excellent base services.'[30] In the words of the Deputy Assistant Secretary of Defence of Installations, 'our policy is to provide excellent barracks, not minimum barracks.'[31] By identifying the army personnel as their customers, it is easy to see how their job is simplified and satisfaction is readily measured. The drawbacks of such an approach, however, are that the taxpayer may be paying for higher standards than they think are appropriate and the local communities may not be receiving the consideration they should while the unit's loudest customer is getting more new accommodation, which does not meet the overall definition of good government. Therefore, more attention needs to be paid to the department's direct contacts, recognizing that they may be separate from whom they are meant to serve.

Applying Osborne and Gaebler's streamlined mission to the Oil Division of the Department of Energy, the objective might be to provide for efficient licensing and regulation of the North Sea. If their customers are identified as the oil companies though, which is effectively the case at present, the meaning of efficient will be quite different than if the customers are British oil consumers or tax payers. There is no right answer and these decisions are not easy to make. Most importantly, if the decision is left to the civil servants, they may select the group with whom they come into the most contact and who are most able to complain to their political masters if they are displeased.

Osborne and Gaebler do recognize that setting up corresponding structures and

[30] Osborne and Gaebler, *Reinventing Government*, p.134.

[31] Osborne and Gaebler, *Reinventing Government*, p.135.

rewards are necessary in order to sustain the desired changes.[32] But these points too need careful attention. As the finding is this case highlighted, civil servants have distinct sets of motivations. Therefore, some of Osborne and Gaebler's recommendations that are adapted from business are not likely to work with civil servants. For example, they suggest that introducing competition into the bureaucracy and holding out deregulation as a reward for individuals will improve performance. But civil servants who have purposely chosen government service because it offers a secure environment may not respond as Osborne and Gaebler suggest. In fact, such measures may decrease the sense of being part of the government policy-making and reduce access to ministers, thereby diminishing two of the main factors that make work 'interesting' for civil servants, and in turn reducing their incentive to cooperate or even stay in the civil service. The structure would then compete with the private sector for employees, and attract civil servants on the basis of salary on which the government is notoriously uncompetitive. Instead, a superior's recognition or additional responsibilities may be simple measures that will more directly achieve the goals of greater efficiency and higher quality service. These changes will be most effective in flexible bureaucracies where individuals are career-maximizers and thus responsive to interesting work and career advancement opportunities.

Other suggestions that may have unintended effects are the de-centralization of government, and the allocation of more power to those dealing directly with the public.[33] In an extreme sense, this is what the British government has been creating

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[32] Carver and Vondra, 'Reinventing the Business of Government: An Interview with David Osborne,' p.140.

[33] Osborne and Gaebler, *Reinventing Government*, Chapter 9.

with quasi government agencies. Such de-centralized units would presumably have permanent staffs and organizational autonomy yet little financial independence. As such, the officials would not have the option to move to other governmental departments. Using the findings of how civil servants in inflexible bureaucracies and managers in state-owned industries act, it is possible to hypothesize that the officials will be very committed to their organization and seek to increase the organization's financial independence as part of a strategy to direct the agency's resources to increase their own well being. They will also pursue other self and budget maximizing strategies to enhance their current situation, but will be concerned with the long-term implications of their actions because they may still be there and called to responsibility in the long-term. They will proceed without regard for broader governmental implications, such as expense or conflict with other departments, because those are beyond their realm of responsibility.

Studies such as Osborne and Gaebler's focus on bureaucracies, when instead the real problem is the short-term horizons of their political leaders. As Neal Peirce, a leading U.S. columnist on state and local government notes:

> Indeed, there are not a few cynics who say that legislature and future planning mix like oil and water. The reasoning is that legislators' lives revolve around the election cycles. Politics forces them to be preoccupied with district and regional problems, to go for fast short-term payoffs instead of thinking and acting long-term.[34]

Neither bureaucrats themselves nor reform of the bureaucratic system alone can transform short-term policies into efficient and effective long-term practices.

Even though these studies highlight the importance of leadership, they do so only in

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[34] As quoted in Osborne and Gaebler, *Reinventing Government*, p.235.

connection with motivating bureaucrats.[35] The problem is more than just bureaucratic leadership; it is the policies that bureaucrats are given to implement. And politicians have little incentive to change this situation as they have been successfully elected under the current system.

Though considerable thought has been given to this problem, there are few satisfactory solutions.[36] The findings from this British case study suggest three areas where more work can be done on long-term political accountability. These include the role of policy entrepreneurs, how to bring forward the long-term costs of politicians' party political calculations, and how to improve the quality of public demand to incorporate long-term needs.

Conclusions

A government voluntarily relinquishing control of valuable national assets is not a rational act - at least when examined as a whole from the macro-level. But when the act is broken down into pieces, and factors are isolated at different levels of analysis, the pieces of the process can be understood as rational. Incorporating several aspects of the micro-level is important as a one dimensional analysis is insufficient. For example, normally policy entrepreneurs are politicians, or leaders of interest groups (Olson, 1971). But by only focusing on the politicians, it is possible to miss the fact that policy entrepreneurs can also be business executives and officials

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[35] Osborne and Gaebler, *Reinventing Government*, p.235-49; and John Dilulio, Gerald Garvey and Donald Kettl, *Improving Government Performance: An Owner's Manual* (Washington, DC: Brookings Institution, 1993).

[36] Dunleavy, *Democracy, Bureaucracy and Public Choice*, p.235-49; and Osborne and Gaebler, *Reinventing Government*, p.136-44.

in international organizations, as BP managers and the IMF top officials were during the 1977 BP sale. The changes in structures from the international level to the company level to the bureaucracy all were able to affect the policy outcome. This illustrates that it is not possible to predict rational policy outcomes from a macro-level, as these level-specific factors resist generalization.

In their own way, each set of actors along with the changes in the corresponding structures set the parameters for the government's decision to sell its oil assets. The connection of these influences can be illustrated with Venn diagrams where each circle represents the overlap of factors at its level. Thus, circle 1 represents the area where the parameters from the international economy overlapped with the international oil industry and membership in international organizations. While the levels and influences exist in three dimensions, imagine them being placed on top of each other as if looking down from the top of a funnel. The location of these parameters are illustrated for 1974, 1979 and 1982 (see Figures 8.1, 8.2 and 8.3). Circles 1-4 in descending size respectively represent the combined factors of the international, company, bureaucracy and political process levels. The points represent specific policy options: point A to increase taxes, point B to increase the budget deficit and point C to sell oil assets.

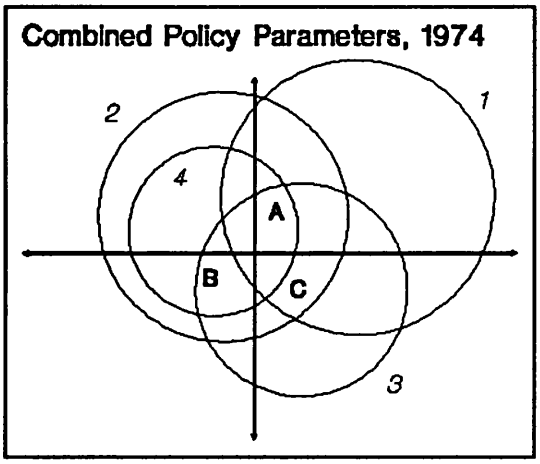

Figure 8.1.

In 1974, just after the 1973 oil crisis and before North Sea oil was in production (and before BNOC was even created) the structures of the international

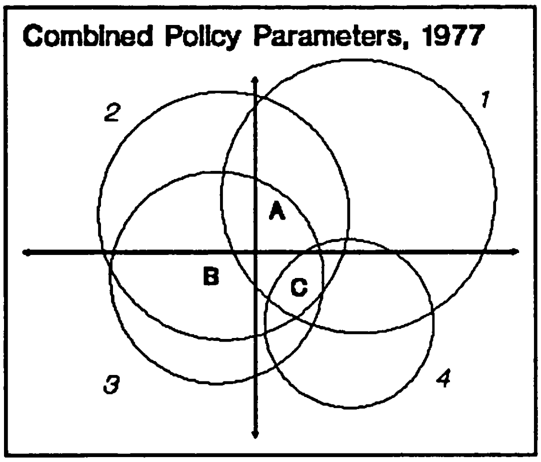

Figure 8.2.

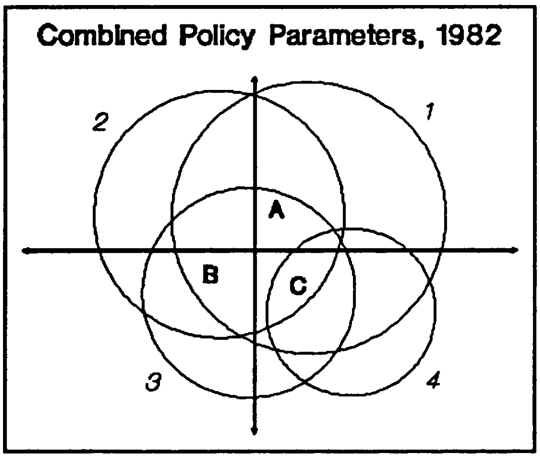

Figure 8.3.

oil industry and public demand were such that a sale of oil assets was not possible (as represented by the exclusion of point C from circles 1 and 4) as represented in Figure 8.1. In 1977 the situation had changed so that asset sales were within the international and policy parameters while the option of a budget increase was prevented by the IMF and the international financial community (point B excluded from circle 1), while a policy of new taxes was restricted by domestic political opposition (point B excluded from circle 4), as represented in Figure 8.2. An asset sale was thus the only one of the three policies possible (only point C in overlap of circles 1-4). In 1982, again the options changed, where all three options were possible at the international, company and bureaucracy levels (points A, B and C in circles 1-3), but only assets sales fit the Conservative's political supply-side factors (only point C in circle 4), and again, an asset sale was the only one of the three policies possible (only point C in overlap of circles 1-4) as represented in Figure 8.3.

Looking at all four levels provides a much richer and more accurate understanding of the purpose and the effect of asset sales in Britain. Though the multi-level approach is perceived as the struggle of the modern political scientist, the importance of including layers of analysis is not new. In fact, returning to the original study of states as actors, closer examination reveals that Thucydides greatest contribution with *The History of the Peloponnesian War* may be the importance of multiple perspectives to enhance knowledge about politics, and his legacy to realists may be misinterpreted. Laurie Bagby and others have argued that Thucydides' emphasis on the state has been over emphasized and that scholars have ignored the depth of his account which includes significant recognition of the role of specific national and individual factors.[37]

While many authors have made laundry lists of factors that cause privatization, few if any are melded into coherent theories.[38] By incorporating constraints more systematically into our analysis of individual actors, hopefully I have moved beyond March and Olsen's first step:

> The institutionalism we have considered is neither a theory nor a coherent critique of one. It is simply an argument that the organization of political life makes a difference.[39]

Adopting a public choice framework and focusing on the individual while also assimilating the constraints they face at four levels, I propose a more systematic way of incorporating several variables at the same time. This approach also suggests a logic for focusing on the most significant policy determinants. Though losing the

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[37] Laurie M.Johnson Bagby, 'The Use and Abuse of Thucydides in International Relations,' *International Organizations*, Vol.48, No.1, Winter 1994, pp.131-53.

[38] Vickers and Wright, 'The Politics of Industrial Privatisation in Western Europe'; Sulieman and Waterbury, 'Introduction: Analysing Privatization in Industrial and Developing Countries'; Heald, 'The United Kingdom: Privatisation and its Political Context'; Dunleavy, 'Explaining the Privatization Boom'; and E.S. Savas, *Privatization: The Key to Better Government* (Chatham, NJ: Chatham House, 1987).

[39] March and Olsen, 'The New Institutionalism,' p.747.

parsimony of a single level analysis, this approach retains consistency by focusing on the individual unit throughout. The depth of understanding gained in the trade-off is worthwhile, as no other approaches have satisfactorily explained state disengagement.

This case of Britain's oil asset sales has also demonstrated that despite much work in the field of public choice theory, some of the basic assumptions still need to be refined in order to recognize that bureaucrats are not just budget-maximizers in pursuit of pecuniary benefits, but rather that they also value other goods such as interesting work, and that they pursue career-maximizing strategies. Furthermore, it must be emphasized that policies are led by supply as well as demand factors. This case reveals that there are still important areas that have not been fully addressed, including the role of international factors, the role played by the managers of nationalized industries, the use of individual strategies by bureaucrats, and the contribution of political supply-side factors make to policy-making, including policy entrepreneurs, cost-benefit analyses and demand of party supporters.

Appendix I: Chronology of Events

1908: Oil is discovered in Persia by a syndicate of the Burmah Oil Company, the Anglo-Persian Oil Company (APOC)

1911: United States Supreme Court orders the dissolution of Standard Oil Trust

1914: The British government purchases a majority holding in APOC

1914-18: World War I and the mechanization of the battlefield

1920-23: The British Government considers selling its holding in APOC

1922-28: Negotiation of the "Red Line" and the "As-Is" agreements

1932-33: Shah Reza Phavli cancels Anglo Iranian Oil Company's (AIOC) concession; AIOC wins it back

1934: AIOC and Gulf gain joint concession in Kuwait

1938: Mexico nationalizes its oil companies

1939-45: World War II

1950: Fifty-fifty (participation) agreement between Aramco and Saudi Arabia

1950: Mohammed Mossadegh nationalizes AIOC assets in Iran

1951-53: Korean War

1953: Mossadegh is overthrown and the Shah returns to power. The management of Iraqi oil operations is contracted to an international consortium and AIOC obtains a 40 per cent majority stake

Reports surface that the Conservative government is to dispose of its 56 per cent holding in AIOC

1956: Colonel Gamal Abdel Nasser of Egypt announces the appropriation of the Suez canal

1957: European Economic Community established

1960: Organization of Petroleum Exporting Countries founded in Baghdad

1964: First round licenses are awarded for exploration in the North Sea by the Department of Trade and Industry

1965: British Petroluem (BP) discovers gas in the North Sea

1965: Britain imposes sanctions against Rhodesia

1967: Six Day War, Suez Canal closes

1967: Government's shareholding in BP drops below the 50 per cent mark to 48.2 per cent

1968: Oil is discovered on Alaska's North Slope

1968: Prime Minister Harold Wilson announces the end of British military presence in the Persian Gulf, completed by 1971

1969: Oil is discovered on the Norwegian side of the North Sea

1970: Oil is discovered on the British side of the North Sea by BP

1972: Gas Act creates the British Gas Corporation from the Gas Council

1973: Britain joins the European Community

1973-74: AOPEC countries cut back supplies to the United States and the Netherlands

Shell and BP refuse to give Britain preferential treatment in the supply of oil

1974: The Department of Energy is established

International Energy Agency is founded

1975: Government's shareholding in BP increases from 48 per cent to 68 per cent through the purchase of Burmah's holding in BP

First North Sea oil lands in Britain

1976: The British National Oil Corporation is established

1977: First sale of oil assets: British government sells 17 per cent in BP, reducing its shareholding from 68 per cent to 51 per cent

1979: Government sells another 5 per cent shareholding in BP, reducing its holding to 46 per cent

Iranian revolution - Shah Reza Pahlavi goes into exile and Ayatollah Khomeini takes power

1980: Iraq launches war against Iran

1981: British oil production in the North Sea surpasses domestic consumption

1982: OPEC agrees to first quotas

BGC is instructed to sell its stake in the on-shore oil field, Wytch Farm

Oil and Gas (Enterprise) Act enabled the government to sell BNOC and BGC's oil assets

BNOC split: production half becomes Britoil, 51 per cent is sold to the public

1983: Britain becomes the sixth largest oil producer in the world

BGC's oil assets are sold as Enterprise Oil

Government sells another 15 per cent shareholding in BP, reducing its holding to 31.5 per cent

1984: BGC's interest in Wytch Farm is finally sold

1985: Government sells remaining stake in Britoil

BNOC is disbanded, replaced by the Oil and Pipelines Agency

1986: Oil price collapses

1987: Government sells its remaining shares in BP in the midst of the October stock market crash

1988: BP takes over Britoil

Cease-fire in Iran-Iraq War

1993: Department of Energy re-merges with the DTI

Appendix II: The Bradbury and Bridges Letters

The Bradbury Letter

Treasury, Whitehall, S.W.
20th May 1914

Gentlemen,

With reference to the Financial Agreement which has been duly settled on behalf of His Majesty's Government and sent to you company for signature, I am directed by the Lords Commissioners of His Majesty's Treasury to offer the following observations regarding the provisions of the amendments proposed to your Articles of Association:

1. By the Article 91A it is provided than an ex officio director shall have the right to negative any resolution which may be proposed at a board or committee meeting, but that the other directors, or a majority of them, shall have the right to appeal there from to His Majesty's Government, which, for the purpose of the Article, is defined as meaning the Treasury and Admiralty. His Majesty's Government, which, for the purpose of the Article, is defined as meaning the Treasury and the Admiralty. His Majesty's Government are of opinion that it would not be prudent, or, indeed, practicable, to qualify the generality of the right of veto. On the other hand, it is felt that the ordinary directors (meaning by that expression the directors other than the ex officio directors), and incidentally the members of the company, should have some safeguard in the matter. It is thought that the right which is to be given by the new Article to the ordinary directors of appealing to the two Departments will afford the requisite safeguard. The ordinary directors will, by appealing to the Departments, be in a position to ensure in regard to any particular question that the right of veto is not exercised until the question has been considered and adjudicated upon by the Departments.

I am to add that His Majesty's Government do not propose to make use of the right of veto except in regard to matters of general policy, such as -
(1) The supervision of the activities of the company as they may affect questions of foreign, naval or military policy;
(2) Any proposed sale of the company's undertaking of proposed change of the company's status;
(3) The control of the new exploitation, sites of wells, etc.;
(4) Sales of crude or fuel oil to foreigners, or such exceptional sales to other persons on long contracts as might endanger the due fulfilment of current Admiralty contracts;

and that their interference (if any) in the ordinary administration of the company as a commercial concern will be strictly limited to the minimum necessary to secure these objects. Further, in the case of any such interference, due regard will be paid to the financial interest of the company is which, under the proposed arrangements the Government have themselves so large a stake.

While His Majesty's Government are not prepared to enter into any binding agreement in regard to the exercise of the veto, you are at liberty to treat the above as an assurance as to the general lines upon which they will act in the matter, not only in regard to the Anglo-Persian Company, Limited, but also in regard to the subsidiary companies.

2. By the word added to Article 96 it is provided that the ex officio directors shall be members of every committee of the board. His Majesty's Government do not however, contemplate that both the ex officio directors should always be present at committee meetings. Occasions may arise when it may be desirable that both the ex officio directors should be present, but as a general rule the presence of only one of them would be necessary. Indeed, at some meetings it may not be necessary that either of them should be present.

3. You are at liberty to make such use of this letter as you may think fit at the proposed meetings of the shareholders.

I am, Gentlemen,
Your obedient Servant,
(signed) John Bradbury

Messrs. The Anglo-Persian Oil Company, Limited

Winchester House, Old Broad Street, London E.C.

(As reprinted in Hansard, House of Commons 1928-29, 26 March 1929, Vol.226, col.2263-4.)

The Bridges Letter

12 April 1951

Gentlemen,

I am directed by the Lords Commissioners of H.M. Treasury's concern to recent developments in Persia and their possible effect on the Anglo-Iranian Oil Company. H.M. Government have in mind not only their own large financial interest in the Company, but the vast importance of the Company's operations to the economy of the United Kingdom, and indeed to the Sterling area as a whole.

The relationship between H.M. Government and the Company forms the subject of the letter sent by Sir John Bradbury to the Company on the 20th May, 1914, following the signature of the Financial Agreement between H.M. Government and the Company of the same date. H.M. Government do not feel that it is necessary to amend the terms of Sir John Bradbury's letter. While recognizing the close co-operation that has existed between H.M. Government and the Company, they feel sure that the Company will appreciate that it is more than ever necessary, particularly in the present critical circumstances, for H.M. Government to be kept in close touch with the development of the Company's general policy and above all that there should be mutual consultation in good time, and at the appropriate levels, about any developments likely to effect substantially the Company's position in Persia or in other territories where it has a concessionary interest.

I am, Gentlemen,
Your Obedient Servant,
(signed) Edward Bridges

(As reprinted in Hansard, House of Commons, 16 February 1977, Vol.926, col.270-1.)

Appendix III: Research Methods

Although there is a wealth of writing about privatization in Britain, most has focused on the economic advantages and disadvantages of privatization rather than the political rationale. As such, there has been little concern for how the sales were decided and implemented and who was involved. Many authors who have written on privatization have focused on the later stages of the policy and have relied on published governmental reports and newspaper accounts as source materials, their conclusions are not as focused or detailed as the account here.[1] To avoid this shortcoming, much of the information gathered for this study comes from over 50 interviews with those involved in the sales including oil company executives, civil servants and politicians. Since many of the details were never previously made public, the interviews were invaluable both for ascertaining a record of what actually happened and who was involved, and for the opinions, perceptions and motivations of the various actors.

I started my study with a review of secondary sources as well as government and company documents, and began my interviews at the end of the first year. In tandem with my data collection, I developed the theoretical side of the thesis. While the theoretical part was firmed up more quickly than the factual, it was important to develop the two concurrently, as the theoretical suggested new avenues to pursue while the factual suggested ways in which the theoretical needed to be reconsidered.

[1] Nelsen (*The State Offshore Petroleum, Politics and State Intervention*) however includes 32 interviews with British civil servants and oil company executives in his comparison of British and Norwegian oil policy; and Klapp (*The Sovereign Entrepreneur*) interviewed 150 officials in four countries.

Interviews:

My plan for the interviews was to start with the retired and less senior oil company executives and then move to the more senior and presumably busier and then repeat a similar cycle with the civil servants and politicians. Using lists of board members and company and departmental organizational charts, I identified those most likely to be involved in the privatization of the British government's oil assets, obtained their biographies and addresses from *Who's Who* and began to contact them. In each case, I sent a letter explaining who I was, the focus of my research, and why it was that I wanted to speak with them in particular, mentioning any relevant connection, such as a recommendation from a previous interviewee or their being an LSE governor. If I had a phone number, I would follow up the next week, which was the most effective technique. If I did not have a telephone number, I had to wait for a reply, which was more likely to be negative; 7 of the 12 written replies were negative whereas only 9 of the 58 telephone contacts were so.

Fortunately, through the good offices of a friend, I was afforded the opportunity to speak to the former chairman of BP, Sir Eric Drake, at the end of my first year of research. He was immensely helpful with the background and players, and gave me referrals to several other BP executives. This made the next round of BP executives more accessible than they might otherwise have been. Once establishing a critical mass of interviews, I was able to parlay them to a total of 53 interviews from October 1991 to March 1994.

It was normally most convenient for the interviewee to meet at their premises, which entailed quite a bit of travelling throughout London, and beyond. Though I did conduct four telephone interviews, I found that a meeting in person was much more fruitful in terms of the time they would devote to the subject and the depth of the conversation, and was therefore worth the extra effort. I was pleasantly surprised by the generosity of the interviewees, both in terms of time and information as well as the occasional tea or lunch. I also found that the further I had to travel, the greater the reward, with the most special being an ox-tail lunch with Philip Shelbourne in Salisbury, one year prior to his death. I met with as many retired officials as possible, as they had more time and were an invaluable source of background information. This later enabled me to focus on critical person-specific questions when meeting with busier executives or officials.

Prior to each interview, I compiled a list of approximately 10 specific questions directly related to the interviewee's experience. The most effective way to begin, however, was to ask about their general background. Often the interviewee would have a version of the company or the government's general oil policy or privatization that they wanted to tell, and after conveying this context they became more comfortable answering questions. Most of the interviewees saw the oil asset sales as a particularly important time in their careers and for government policy and yet, in many cases, they had not previously been asked for their opinion; thus they were generally pleased to discuss their views. At the end of each interview, I asked if there were any points or issues that I missed, and occasionally something else would be revealed. Before leaving, I would also ask if there was anyone else with whom I should speak. Many of the same names were raised, though many new names came up in this process, in which case I then probed to find their direct connection to my project in order to qualify their relevance; otherwise my interviews could have continued indefinitely.

I kept a running list of questions, both 'general view' type questions which I asked of everyone, and more specific ones which I raised as I got further into the specifics of the case. Once a specific point was confirmed I crossed it off the list. To confirm a particular point, I either had two interviewees give the same information or an interviewee confirm information recorded in company or government documents or a newspaper article.

I began taping the interviews, which did not seem to inhibit BP or BNOC executives from talking freely. When I started interviewing civil servants and politicians, however, they were ill at ease with the recorder so I soon stopped trying, realizing that it was more important to get a detailed explanation rather than a recorded party line. When unable to tape the interview, I took notes during the meeting and then supplemented these immediately afterwards, adding additional recollections. In every case, I would type a full transcript that day as well as send a thank you note to the interviewee, with an eye to keeping communication lines open for possible further contact. In several cases, I did call back later to investigate a point or ask how to obtain further information, which was very useful.

Of 69 people I approached, 53 agreed to meet with me while 16 declined. For a break down by occupation, see Table A.1., and for a list of all interviewees, see List of Interviewees in Appendix IV. Of those who declined, ten were civil servants, four were politicians and two were the BP directors appointed by the Government. The civil servants were either in high positions in the current government and too busy to meet, or felt that they were not closely enough involved in the oil asset sales to be useful to my research. The 4 politicians were Margaret Thatcher, Geoffrey Howe, Tony Benn and Alexander Eadie. Thatcher, in particular, would have been an important addition but despite two attempts to get her on record, she declined. (See Exhibit A.2.). The only other obstacle to interviewing was at Enterprise Oil, where only one executive agreed to speak as the representative of the company: 'I'm the person you will speak to here. I will represent us.'[2]

Table A.1. Interviews by Category

Treasury civil servants	7
DEn civil servants	12
BP executives	10
BNOC executives	14
BGC executives	2
Politicians	7
CPRS officials	5
* Total Interviews	53

* While the total number of interviews was 53, the total number of categories is greater as several interviewees served in more than one category, i.e. a civil servants served in both the Department of Energy and the Treasury.

Qualitative Computer Analysis

To aid in the collation of this information and to cross check sources, I used the qualitative computer analysis programme, Non-numerical Unstructured Data

[2] Interview with Department of Energy civil servant and Enterprise Oil executive. (West)

Indexing, Searching and Theorising (NUDIST).[3] In the typed transcripts, I went back through and labelled each paragraph or point made in the interview with a key word, and then copied the transcript into a NUDIST raw-file. In addition, I added notes from other sources, primarily politicians' memoirs, detailed accounts of the time period and notes from the *Times*, the *Financial Times*, the *Economist*, and the *Petroleum Economist*, again labelled with key words.

NUDIST works by building trees of information. The trees I developed are shown in Figure A.1. By sorting by these categories, I was able to gather together all the information on that topic and systematically compare facts and views. This was more efficient than note cards because the whole context of the point could be included and a point could also be listed under several different categories.

While more efficient that manual collation, NUDIST is a slow and cumbersome programme. In part, this is because it was developed originally for Macintosh computers by a group of academics in Australia and only later was adapted for a Windows/IBM environment, the version available at LSE, which made it considerably slower. I was able to write automatic command programmes to avoid waiting through the sorting process, though the input and retrieval of information was still a very time consuming process. One glitch in the process was that the results files that NUDIST produced were not immediately compatible with Word Perfect, and had to be first transferred to another word processing programme for formatting.

[3] Thomas Richards, Lyn Richards, Joan McGalliard and Boyd Sharrock at La Trobe University, Burndoora, Australia. References: *NUDIST 2.3 User Manual*; and *NUDIST 2.3 Reference Manual*, 1992.

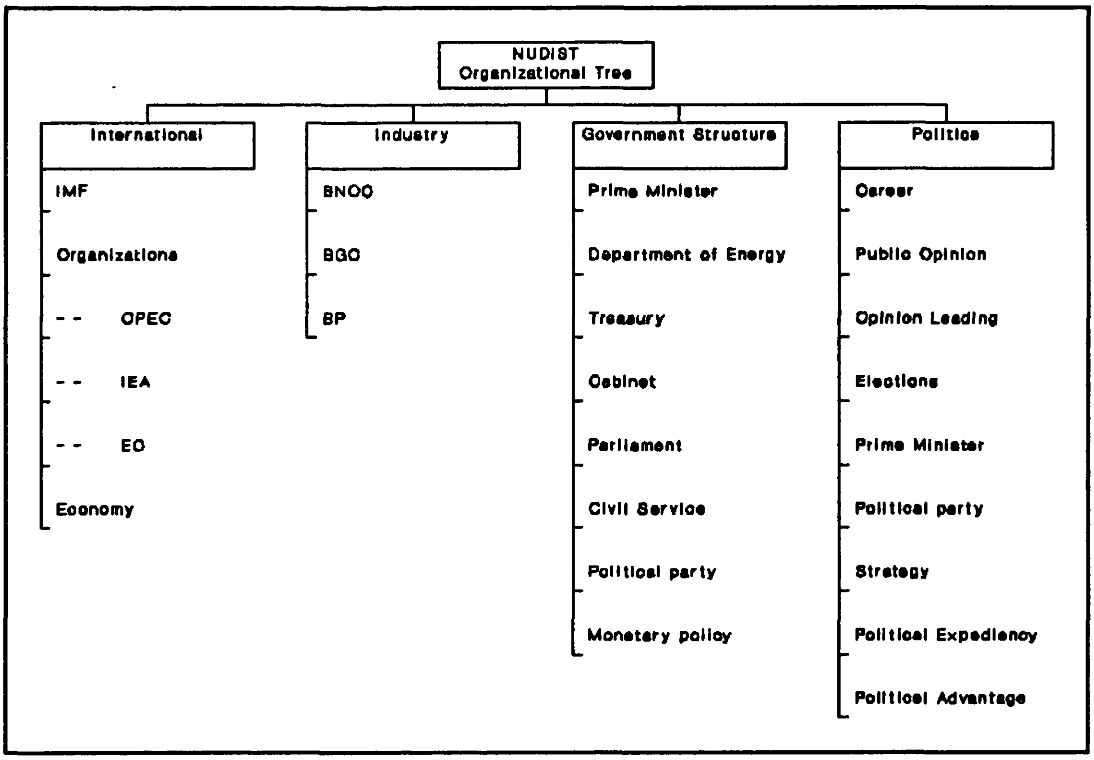

Figure A.1.

Literature

The literature used in this research included annual reports, government publications, newspapers and journals, public opinion polls, and the memoirs of some of the politicians at the time; I also relied on secondary sources, but primarily for background information for the many different levels that I have incorporated in this study. I was greatly aided by electronic information technology: The database of the Financial Times' Profile service enabled me to search systematically through the *Times*, the *Economist*, and the *Financial Times* from 1982 to 1990 using key words such as: BP, BNOC, Britoil, Enterprise Oil, Wytch Farm and privatization, assurances, golden share, KIO and BP. I realized the value of this source after manually looking up these same key words in the *Times* index and then searching for the articles on microfilm from 1974 to 1981. I also searched manually through the *Petroleum Economist* from 1980 to 1988. I was also able to use the file of newspaper clippings kept by the Institute of Petroleum on specific oil issues which included a wider range of daily newspapers than I was able to search on my own.

Though current years of *Hansard Parliamentary Debates* are now on electronic data bases, the years with which I was concerned were not. Therefore, going back to 1911, I surveyed all references to BP (including APOC and AIOC), BNOC, Britoil, Wytch Farm and Enterprise Oil, as cited in the annual index for the Commons and Lords debates and questions from 1911-1988. Similarly, I reviewed all the Parliamentary Select Committee meeting minutes and reports after 1976 that pertained to BP, BNOC and Britoil, BGC, Enterprise Oil and Wytch Farm; and the official Acts, including the Gas Act of 1972 and the 1982 Oil and Gas (Enterprise) Act.

Company documents included annual reports, financial accounts, sale prospectuses and occasional publications. Some of those I interviewed also gave me references to articles in more specialist journals that reinforced the point they were making. I also had the great fortune of being given access to confidential company and government documents early on in the research process. The information revealed discussions which most interviewees had denied. This event heightened my scepticism of what the interviewees said and also helped me to recognize that certain types of information were only known at certain levels.

The one source I was unable to examine was *A Finding of Departmental Experience: A History of Government Involvement in North Sea Oil* written by John Liverman in 1982. Several of those I interviewed referred to the book, but those with access claimed it was not available to the public, and I never was able to see it. The denial of access became particularly frustrating when one civil servant actually looked up some information in it during my interview, but would not allow me to examine it. Daniel Yergin records in his notes on *The Prize* that he was able to read the document in the Department of Energy as long as he did not take notes; I was not afforded this same opportunity. Through my interviews as well as Yergin's work, though, I doubt there is anything relevant to my project in Liverman's study that I did not uncover.

The other types of existing literature that I used were public opinion polls. While they are used frequently by many academics, I found it useful to review them first hand to examine both what they recorded and what they did not; specifically when and whether public opinion polls were held on privatization or state ownership, and the intensity of that opinion. This entailed searching systematically through MORI and Gallup Polls of British Public Opinion from 1976 to 1988. Using the index of *British Opinion Polls 1960-1988* I found all polls on privatization, nationalization and public ownership during the time period.[4] I also recorded general public opinion trends on issues, leaders and parties every six months from 1976 to 1988. By looking systematically through these polls, I realized privatization seldom merited a single question or a mention on the list of most important issues - indicating a very different image than the responses to the occasional poll revealed.

[4] David Taylor, ed., *British Opinion Polls 1960-1988*, Volume I: Subjects and Names Index, alphabetical and Volume II: Subjects and Names Index, date order, (Reading: Research Publications, 1990).

Exhibit A.1.

MARGARET, THE LADY THATCHER, O.M., P.C., F.R.S.

HOUSE OF LORDS

LONDON SW1A 0PW

7th March 1994

Dear Ms Hoopes

Thank you for your letter of 22nd February enclosing your further letter to Lady Thatcher.

I have discussed your request with Lady Thatcher and I am afraid the answer must remain negative. As I stated in my original letter she receives many requests similar to yours and she is not able to accede to them all. Lady Thatcher's schedule for the next few months is immensely busy with overseas lecture tours, and work on the second volume of her memoirs, that she is simply not in a position to accept any more commitments. She is sorry to have to send another disappointing response but hopes you will understand.

Yours sincerely

M. Granger

MIRANDA GRANGER
Private Office

Ms S M Hoopes

Appendix IV: List of Interviews

Interview with Robert Adam, 6 August 1992.
BP 1950-83; Director, BP Trading, 1973-75; Director, Sohio, 1972-76 and 1978-83; Managing Director Finance, BP, 1975-83 and Deputy Chairman 1981-83.

Telephone Interview with Sir Lawrence Airey, 3 February 1993.
HMG 1949-79, HM Treasury, 1958-79, Second Permanent Secretary 1977-79; Member, BNOC, 1976-77; Chairman, Board of Inland Revenue, 1980-86.

Interview with Sir Fred Atkinson, 22 February 1993.
HMG 1949-79: Treasury, 1955-62 and 1963-69; Foreign Office, 1962-63; Ministry of Technology, 1970; Chief Economic Advisor, DTI, 1970-73; Assistant Secretary General, OECD, 1973-75; Deputy Secretary and Chief Economic Adviser, Department of Energy, 1975-77; Chief Economic Adviser, Treasury, and Head of Government Economic Service, 1977-79; Co-author: *Oil and the British Economy*, 1983.

Interview with Dr. Leslie Atkinson, 7 October 1992.
Seconded from BP to CPRS October 1977 to August 1979.

Interview with Lord Joel Barnett, 4 March 1993.
MP (L) Heywood and Royton, 1964-83; Member Public Accounts Committee, 1965-71, and Chairman, 1979-83; Opposition Spokesman on Treasury matters, 1970-74; Chief Secretary to the Treasury, 1974-79; Cabinet Member, 1977-79; House of Lords, 1983-; Opposition spokesman on the Treasury in House of Lords, 1983-86.

Telephone Interview with Ken Berrill, 15 July 1993.
Advisor to the Treasury, 1967-69 and 1973-74; Head of CPRS, Cabinet Office, 1974-80; Chairman, Vickers de Costa, 1981-85; Chairman, SIB, 1985-88; Deputy then Chairman Robert Horne Group, 1982-90; and Chairman, Commonwealth Equities Fund, 1990-.

Interview with Penny Boys, 11 June 1993.
HMG 1969-89: Department of Energy, 1973-78; seconded to BNOC 1978-80; Head of International Unit, Department of Energy 1981-85; seconded to Treasury, 1985-87; Director of Personal, Department of Energy, 1987-89; Deputy Director General, Office of Electricity Regulation, 1989-.

Interview with Dr. John Buchanan, 30 April 1993.
BP executive, seconded to CPRS 1976-77.

Interview with Graham Campbell, 8 February 1993.

HMG 1949-84: Ministry of Fuel and Power, 1949-65; Under Secretary, DTI, 1973; Under Secretary, Department of Energy, 1974-84.

Interview with Ian Clark, 9 April 1992.

Member BNOC 1976-82, trading, participation, Joint Managing Director, Britoil 1982-85.

Letter from Gerry Corti, 11 May 1992.

Department of Energy, mid 1970s; executive, BNOC, early 1980s; Author, *A Nation's Oil.*

Interview with Lord Croham, 29 April 1992.

LSE, BSc (Econ), 1938; HMG, 1939-74; Treasury 1960-64, Department of Economic Affairs, 1964-68; Permanent Secretary, Treasury, 1968-74; Head of Home Civil Service, 1974-77; Deputy then Chairman, BNOC 1978-85; advisor to the Bank of England, 1978-83; Chairman, Guinness peat Group, 1983-87.

Interview with Roy Dantzic, 23 April 1992.

Samuel Montagu 1974-80, Member for Finance, BNOC, subsequently Finance Director, Britoil 1980-84; Director, Wood Mackenzie, 1985-89, Chairman Saxon Oil 1984-85, Part-time Director, BNFL, 1987-91.

Interview with Derek Davis, 27 July 1993.

HMG 1967-: Secretary, Energy Committee, 1977-79; NEDC Energy Task Force, 1981; seconded to NCB, 1982-83; Under Secretary, DTI (formerly Energy) 1987-.

Interview with Edmund Dell, 2 March 1993.

MP (L) Birkenhead, 1964-79; Paymaster General, 1974-76; Chairman, Public Accounts Committee, 1973-74 (Acting Chairman, 1972-73); Director, Shell Transport and Trading, 1979-; Chairman and Chief Executive, Guinness peat Group, 1979-82; Founder Chairman, Channel Four TV, 1980-87.

Interview with Sir Eric Drake, 17 October 1991.
Letter from Eric Drake, 24 October 1991.

BP, 1935-75: Chairman, 1969-75; Court of Governors, LSE, 1963-74; and Hon. Petroleum Advisor to the British Army, 1971-.

Interview with Jeremy Evans, 20 March 1992.

HMG 1960-76: Ministry of Technology, 1970-74; Department Director of Offshore Supplies Office, 1973; Department of Energy, 1974-76; seconded to BNOC, 1976-78; Managing Director, BNOC 1978-82, Member, Board of Directors, 1981-82; Director, Britoil, 1982-88; British Rail, 1990-.

Interview with Sir Alistar Frame, 1992.
UKAEA, 1964-68; RTZ, 1968-91: Chief Executive and Deputy then Chairman, RTZ, 1978-91; Director, Britoil, 1983-84.

Interview with Patrick Gillam, 16 September 1992.
BP 1957-91: General Manager, Supply Dept 1974-78; Director, BP International, 1978-88; Managing Director, BP, 1981-91; Court of Governors, LSE, 1989-.

Interview with Ian Goskirk, 28 July 1992.
Shell International Petroleum, 1956-74; Anschutz Corp, 1974-76; BNOC 1976-85: Managing Director, BNOC Trading, 1980-82; Chief Executive, BNOC, 1982-85; Director, Cooper and Lybrand, 1986-90, Partner, 1990-.

Interview with Lord Hamish Gray, 7 June 1993.
MP (C) Ross and Cromarty, 1970-83; Asst Government Whip, 1971-73; Lord Comr, Treasury, 1973-74; Opposition Whip, 1974-75; Opposition Spokesman on Energy, 1975-79; Minister of State, Department of Energy, 1979-83; Scottish Office, 1983-86; Government Spokesman on Energy, House of Lords, 1983-86.

Interview with Alan Gregory, 29 July 1992.
BP 1971-78: Director, UK and Ireland Region, 1980-85; Director, BP Chemicals International, 1981-85; Director of Government and Public Affairs, 1975-85.

Interview with John Guinness, 1 September 1993.
HMG, 1962-; CPRS 1972-75 and 1977-79; Foreign Office then Foreign and Commonwealth Office 1962-72; Home Civil Service, 1980; Department of Energy: Under Secretary 1980-83, Deputy Secretary 1983-91; and Second Permanent Secretary 1991; British Nuclear Fuels, 1992-.

Interview with Peter Harding, 27 July 1993.
HMG 1949-91: Department of Energy, 1974-91, Under Secretary, 1989-91.

Interview with Charles Henderson, 23 July 1993.
HMG 1973-: Department of Energy 1974-88, Head of Arts and Libraries 1989-92; Head of Energy within DTI, 1992-.

Interview with David Howell, 25 May 1993.
MP (C), Guilford, 1966-; Minister of State, Department of Energy, 1974; Secretary of State for Energy, 1979-81; Secretary of State for Transport, 1981-83.

Interview with William Jewers, 19 August 1992.
Regional Gas Boards, 1946-68; Director of Finance, Gas Council, 1969-73; BGC: Director of Finance, 1973-76, and Managing Director for Finance, 1976-87.

Interview with David Jones, 11 June 1993.
HMG, 1947-82: Ministry of Power and later Ministry of Technology and DTI, 1947-52 and 1963-73; Cabinet Office, 1976-77; Department of Energy, 1978-82; Director, Long Term Office, IEA, 1982-88.

Interview with Sir Philip Jones, 26 May 1993.
HMG 1955-83: Ministry of Technology, 1967-71; DTI 1971-73; Department of Energy 1974-83; Member BNOC, 1980-82; Chairman, Electricity Council, 1983-90; Chairman, Total Oil Marine, 1990-.

Telephone Interview with Lord Kearton.
Courtualds, 1946-75, Chairman, 1964-75; Part-time Member, UKAEA, 1955-81; Chairman and Chief Executive, BNOC, 1974-80.

Interview with Sir Peter Kemp, 6 May 1993.
HMG 1967-93: Ministry of Transport, 1967-73; Treasury 1973-87; Permanent Secretary, Cabinet Office, 1988-93.

Telephone Interview with Mr. Khakee, 28 January 1994.
Accountant, DTI, 1983; on loan to Department of Energy since 1986.

Interview with Sir Christopher Laidlaw, 22 September 1992.
BP 1948-81; Managing Director, 1972-81, Chairman BP Oil 1977-81, and Deputy Chairman, 1980-81; Chairman, ICL, 1981-84; Chairman, Bridon, 1985-90; and Director, Amerada Hess, 1983-.

Interview with Gavin Laird, 11 June 1992.
Amalgamated Engineer Union, 1972-; General Secretary (Eng Section), 1982-; Member, Executive Council, 1979-82; Part-time Government Director, BNOC 1976-86; Director, Bank of England, 1986-.

Interview with Lord Nigel Lawson, 15 February 1994.
MP (C) Blaby, 1974-90; Opposition Spokesman on Treasury and Economic Affairs, 1977-79; Financial Secretary to the Treasury, 1979-81; Secretary of State for Energy, 1981-83; Chancellor of the Exchequer, 1983-89; House of Lords, 1992-.

Interview with Lord Harold Lever of Manchester, 6 April 1993.
MP (L) Manchester 1945-79; Paymaster General, 1969-70; Member, Shadow Cabinet, 1970-74; Chairman, Public Accounts Committee, 1970-73; Chancellor of the Dutchy of Lancaster, 1974-79; House of Lords, 1979-; Governor, LSE, 1971-.

Interview with John Liverman, 15 March 1993.
HMG 1947-80: Member, BNOC, 1976-80; Deputy Secretary, Department of Energy, 1974-80.

Telephone interview with Christopher Lucas, 4 February 1993.
HMG 1946-80: Treasury, 1950-70; Cabinet Office, 1970-72; Secretary, NEDC, 1973-76; Under Secretary, Community and International Policy Division, Department of Energy, 1976-80.

Interview with Dickson Mabon, 11 May 1993.
MP (L and Co-op) 1955-81, (SDP) 1981-83; Minister of State, Department of Energy, 1976-79; Chairman RGC (Offshore) 1979-82; Chairman, Indigenous Technology Group, 1984-.

Interview with John McCall, 26 March 1992.
Solicitor, Freshfields, on leave to BNOC from 1976-79.

Interview with Lord John Moore, 22 June 1993.
MP (C) Croydon Central, 1974-90; Vice-chairman, Conservative Party, 1975-79; Parliamentary Under Secretary, Department of Energy, 1979-83; Economic Secretary, HM Treasury, 1983; Financial Secretary, HM Treasury, 1983-86; Secretary of State, Department of Transport, 1986-87; Secretary of State, Department of Social Services, 1987-88; Secretary of State, Department of Social Security, 1988-89; House of Lords, 1992-; Chairman, Credit Suisse Asset Management, 1992-; Member, Court of Governors, LSE, 1977-.

Interview with Sir Alistair Morton, 15 October 1993.
Chairman and Chief Executive, Draymont Securities, 1972-76; Managing Director, BNOC, 1976-80; Chairman, Thames Oil and Gas, 1981-83; Chief Executive, Guinness Peat Group, 1982-87, Director, New London Oil, 1986-; Chairman, Eurotunnel, 1987-.

Interview with Robert Priddle, 26 May 1993.
HMG 1960-: DTI, 1973; Department of Energy, 1974-85; Under Secretary, DTI, 1985-89; Deputy Secretary, Department of Energy (now DTI), 1989-.

Interview with Sir Denis Rooke, 4 August 1992.
Gas Board then Gas Council then British Gas Corporation the British Gas plc: Deputy Chairman 1972-76, Chairman 1976-89; Member: Advisory Council for Energy Conservation 1974-77; and BNOC 1976-82.

Interview with David Sarre, 13 May 1992.
BP 1957-82: Secretary of the Board, 1973-82; Legal Advisor, 1970-78; and Director of Personnel, Safety and Environment, 1979-82.

Interview with Sir Philip Shelbourne, 18 October 1991.
Chief Executive then Chairman, Drayton Corp, 1971-74; Chairman and Chief Executive, Samuel Montagu, 1974-80; Chairman and Chief Executive, BNOC, 1980-82; Chairman, Britoil, 1982-88; Chairman, Henry Ansbacher Holding, 1988-91.

Interview with Sir David Steel, 24 March 1992.

BP, 1950-81: Managing Director, 1965-75; Deputy Chairman, 1972-75; Chairman, 1975-81; Director, Bank of England, 1978-85; Director, Klienwort, Benson, 1985-.

Interview with Ron Utiger, 23 April 1992.

British Aluminium, 1961-82, Chairman, 1979-82; Member BNOC, 1976-80; Chairman, 1979-80; TI Group, 1979-89, Chairman 1984-89; Director, British Alcan Aluminium, 1982-.

Interview with Dr. Paul Vaight, 30 September 1992.

BP executive, seconded to CPRS, 1979-82.

Interview with David B. Walker, 10 June 1992.

BP, 1959-85, Chief Executive, BP Petroleum Development, 1980-82; Chief Executive, Britoil, 1985-88; President, UK Offshore Operators Association, 1982; Chairman, Sun International Exploration and Production Co., 1988-.

Interview with Sir Douglas Wass, 28 April 1993.

HMG 1946-83: Alternate Executive Director, IMF, and Financial Counsellor, British Embassy, Washington, DC, 1965-67; Treasury: 1968-83, Permanent Secretary 1974-83 and Joint Head of the Home Civil Service, 1981-83.

Interview with Julian West, 2 July 1992.

Department of Energy, 1974-83; Private Personal Secretary to Nigel Lawson, 1983; seconded to start Enterprise Oil; Enterprise Oil, 1984-; Member of the Board, 1991-.

Interview with Christopher Wilcock, 27 May 1993.
Telephone interview, 21 January 1994.

HMG 1962-: Department of Energy, 1974-; seconded to Shell UK Ltd, 1982-83; Head of Finance, Department of Energy, 1984-86, Director of Resource Management, 1986-88; Head of Electricity Division, 1991-.

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