

# Government and UK Oil Participation Policy

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## 1. INTRODUCTION

The purpose of this paper is to examine the UK government's attempts to influence the domestic oil industry through the creation of a national oil company (NOC), the British National Oil Corporation (BNOC). The economic theories of politics and bureaucracies facilitate the analysis of the various forces involved in the government policy process. By applying these theories to the policy process and to the government/BNOC relationship an insight into the environment in which government oil participation policy has evolved may be gained.

The paper attempts to analyse the process by which government intervention takes place and the impact of the numerous conflicts and imperfections which tend to distort and confuse government action. This process is of especial importance when examining government policies purporting to protect the "national interest" as has been the case with UK North Sea oil policy.

The "national interest" is a vague concept open to wide interpretation by politicians and civil servants. In discussions of the workings of private markets the self-interest axiom is of central importance as the basis of many hypotheses. When considering government activities however, there has tended to be an implicit assumption of governments being staffed by altruists whose only concern is serving the "public good" or "national interest". In outlining the economic theories of politics and bureaucracies, the first section of the paper establishes the framework in which analysis of the policy process is undertaken. It is assumed that subject to certain constraints, individuals in government are self-interested; they attempt to maximize some personal utility function.

Subsequent sections of the paper trace the development of BNOC from the perception of political need for a policy, to the implementation of policy and, in 1982, the re-structuring of BNOC.

## 2. THE ECONOMIC THEORIES OF POLITICS AND BUREAUCRACIES

Anthony Downs attempts to construct an economic theory of representative government around the concept of the government as a monopoly.<sup>2</sup> He relates the motives of rational, utilitarian individuals involved in the process of government to the political structure of society, in this instance, a democracy. Within the framework of analysing the behaviour of rational individuals as citizens (voters) and in government (politicians) Downs develops two basic hypotheses concerning the operation of the political process in a system of representative democracy.

The central thesis adopted by Downs is that the activities of political parties in a democracy are analogous to those of entrepreneurs in a profit-seeking economy. Entrepreneurs are often assumed to attempt to produce those goods which they consider will gain the most profits in order that their personal objectives and desires may be satisfied. Politicians adopt whatever policies they believe will gain the most votes, similarly to satisfy personal objectives.

Thus Downs' first major assumption is that political parties in a democracy formulate or adopt policies so as to maximize votes. To facilitate the analysis of the implications of this thesis it is assumed that each citizen rationally attempts to maximize his utility income, including that portion of it derived from government activity; this is Downs' second major hypothesis. Moreover, because members of political parties are motivated by the intrinsic rewards of holding public office Downs argues that they will therefore formulate policies as a means to holding office rather than seeking office to carry out pre-determined policies.

There are constraints on the activities of politicians and political parties. The government is considered to operate "in a fog of uncertainty".<sup>3</sup> A voter is acting irrationally by acquiring political information as the marginal cost of gaining

the relevant information greatly outweighs the voter's marginal benefit resulting from the infinitesimal effect of a single, but well informed vote. In addition, because the politician is generally unsure of voter preferences there is a danger of the politician adopting a 'wrong' policy and allowing an opposing politician or political party to capture votes.

A similar constraint is emphasised by Tullock.<sup>4</sup> If a party adopts a wrong policy it may be possible for a minority group within that party to gain control by formulating a separate policy. This is the constraint of intra-party rivalry.

Breton<sup>5</sup>, like Downs, maintains that it is the actual institutional framework of a representative democracy that shields politicians from knowledge of voter preferences and thus creates imperfections in the government policy process. This occurs due to three characteristics of the democratic system in the UK:-

1. Voting Rules, whereby a simple majority rule ignores the strengths of voter preferences.
2. The Length of the Election Period, where a government is elected with a comfortable majority for up to five years the rôle of the Opposition in providing political competition is limited.
3. The degree of full-line supply (i.e. how direct is the voting system), for example, logrolling or vote trading may obscure genuine voter preferences.

Breton argues that over time an increasing amount of media attention is allocated to informing the public about political news. In an election period the cost of acquiring a minimal amount of political information to the individual is virtually zero. Furthermore, an individual's willingness to express a preference may vary over time. "The degree of coercion"<sup>6</sup> is defined by Breton as the difference between the amount of public policies desired by an individual and the amount provided by the government. The larger the difference, the greater is the degree of coercion and the greater is the likelihood that an individual

will attempt to affect his position by influencing the policy process. It is as a result of government coercion and individuals' response to it that governments are informed of citizens' preferences and desires. The individual only indulges in political participation if the coercion applied exceeds the individual's personal "coercion threshold". The individual will then attempt to eliminate coercion by working for political change. This process may result in support for opposition political parties, the formation of pressure groups, migration, demonstrating, voting, etc.

A further imperfection in the policy process is that the democratic system of government in the UK tends to favour producer interests more than those of consumers. Due to the strong common objectives of producer groups combined with the cost of gathering information, a collection of individuals as a producer pressure group are able to articulate clearly their policy preferences to the government. Furthermore, it is likely that senior members of producer groups have personal contacts within government or well established lines of communication with government. The government is itself keen for any indication of public preference and is thus likely to pay more attention to the desires of producers than to consumers whose interests are likely to be more diverse and, due to information costs, more obscure. In addition, Breton argues that people join pressure groups not only because of government coercion but because the pressure group's intrinsic need to survive necessitates it seeking causes and encouraging people to join the group.

Turning to the supply of government policies it is important to consider the rôle of government bureaucracies in the policy process. The government bureaucrat has a crucial relationship both with politicians and with industry.

Niskanen<sup>7</sup> views the relationship between the bureaucracy and its sponsor as a bi-lateral monopoly. However, because there is generally a significant difference in the information available to

the sponsor and to the bureaucracy, the sponsor often cannot exploit its position as a monopsony due to a relative lack of information.

The sponsor is not a profit seeking enterprise and officers within the sponsoring organization (i.e. politicians in government) have many functions to perform and are thus essentially part-time overseers and supervisors of the bureaucracy's activities. On the other hand, the bureaucrat has a stronger relative incentive to obtain information and may work full time in doing so. The bureaucrat is able to select information and to withhold information from the sponsor if it is in the bureaucrat's interests, as he sees them, to do so. Niskanen combines these factors to derive the assumption of a passive sponsor. The sponsor knows the budget it is prepared to grant for a given quantity of services but does not have the incentive nor the opportunity to obtain information on the minimum budget necessary to supply the services.

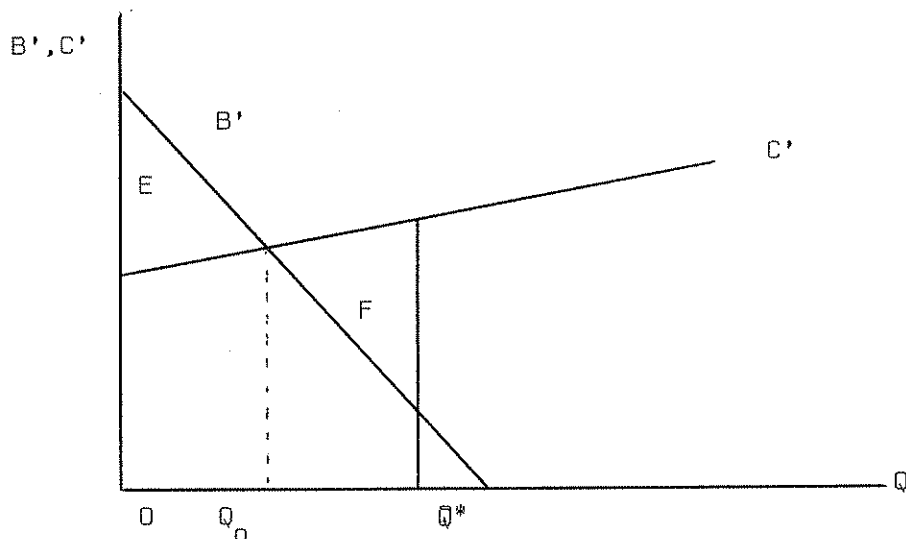
The bureaucrat in Niskanen's model is assumed to be a rational utilitarian who thus attempts to maximize the size of his budget. Although the personal efforts required to manage a bureaucracy are greater the larger is the bureaucracy (or the larger is the budget), an increase in the budget increases the effort required for management by a less than proportionate amount. The bureaucrat's instinct for survival also leads him to maximize the budget size as the bureaucrat's personal workload lessens if the bureaucrat is able to provide increasing budgets for subordinate bureaucrats to offer in salaries and contracts. Furthermore, the nature of the relationship between the sponsor and the bureaucracy is such that the sponsor expects the bureau to expand and seek new programmes and this may necessitate the bureaucracy seeking a larger budget.

The ultimate constraint on the bureaucrat's ambition of maximizing budget size is that the total output of services that the sponsor expects the bureaucracy to provide does not exceed a given

budget. As the bureaucracy exchanges its total service for a total budget the demand function facing the bureau is not a relation between price and quantity but between the marginal value of a service and the level of the service. Because the bureaucracy is a monopoly, its marginal cost function is the marginal expenditure of the bureau at each level of service; it does not supply services at its marginal cost.

Niskanen's model is therefore based on two crucial assumptions. First, that bureaucrats attempt to maximize the size of their budgets and second, that they are monopolists who are able to impose their objectives on their sponsor. This can result in the oversupply of bureaucratic output, illustrated in figure (1). In a Pareto optimal position the bureaucrat would operate at output  $Q_0$  where  $B' = C'$ . However, the bureaucrat seeks to operate at  $Q^*$  where area E equals area F and the bureaucracy captures the equivalent of all the consumer surplus gains of output  $Q_0$ .

Figure (1), The Equilibrium Output of a Bureaucracy



$B'$  denotes the marginal benefit of the policy to the sponsor

$C'$  denotes the marginal cost of the policy to the sponsor

area  $F = \text{area } E$

Source; W. Niskanen, "Bureaucracy; Servant or Master?" (London; IEA, 1973) p.29



The bargaining power of a bureaucracy stems from its ability to withhold information from the sponsor and also on the extent that the information is of a technical or specialist nature, (given that the sponsor/politician is essentially a lay-person in that field). However, it is unlikely that the politician is totally passive as Niskanen suggests. The difference between the budget that the bureaucracy succeeds in obtaining and that desired by politicians is equivalent to the amount of consumer surplus captured by the bureau (area F = area E, figure (1)). Thus the cumulative discrepancy between the actions of the government bureaucrats and the desires of senior politicians may be termed "control-loss"<sup>8</sup>. Politicians may attempt to reduce "control-loss" by the introduction, at some cost, of anti-distortion devices.

By employing some anti-distortion mechanism the politician may be able to reduce, but not eliminate, bureaucratic oversupply. If the cost of the control device is prohibitive, the marginal cost of applying the device is always greater than the marginal benefit from its use, then the outcome is consistent with Niskanen's model. The potential effectiveness of control mechanisms depends on the source of inefficiency within the bureaucracy. To eliminate the oversupply of output the sponsor needs to acquire information concerning the bureau's actual cost curve. If the inefficiency results from X-inefficiency the sponsor must have the information of the bureau's cost curve, plus an estimate of the true minimum cost of supplying the service.

There are limitations to Niskanen's model. It may not be the case that the bureaucrat's utility function is always and everywhere positively and monotonically linked to increases in the bureau's budget size. It may be that a bureaucrat is able to increase his personal stature or career prospects by reducing the bureaucracy's budget size. For the purpose of this paper however, it is important to note that a government bureaucracy may have its own objectives and policy preferences as distinct from those of politicians.

Due to the nature of the bureaucrat/politician relationship, the bureaucrat is able to emphasise characteristics of policy which are consistent with the bureaucrat's own objectives. Moreover, the bureaucrat may be able to use influence in order to understate the importance of policy characteristics which act against the bureaucrat's objectives. Depending on the relative bargaining strength between the bureaucrat and politician, negotiations take place whereby characteristics of policy are traded.

When discussing specific government actions, in this case UK North Sea oil participation policy, a distinction needs to be made between two broad types of policy distortions. First, there is the distortion between an election promise and the implemented policy which results from internal political influences. For instance, a popular political policy in the UK is to control oil production rates in the North Sea. Although the economic wisdom of such a policy is open to considerable doubt, successive governments have adopted this policy apparently because of its attractions as a vote-maximizing policy. The experience of the present Administration has been that it has not felt it can fulfill this election obligation (although there have been some development delays, e.g. in December 1980 the Secretary of State announced the decision to delay the Clyde oilfield project for two years) because it would conflict with other priorities of the government. A further consideration is that as governments hold office for up to five years a party in power may be unwilling to postpone benefits (i.e. oil taxation revenue) which may therefore accrue to a future, and possibly Opposition, government. These internal pressures develop from sources both within and outside Parliament.

Second, there arises the situation when the government, in attempting to implement a policy, confronts a distortion effect from the government department through which the mechanics of the policy are established. It is in this area that the theory of bureaucracy can add to understanding of the government decision-making process. Moreover, theories of bureaucracies are

also relevant to the behaviour of bureaucrats within oil companies. If a policy proposal opposes the interests of a government bureaucrat, the bureaucrat may have the ability (due to the politician/bureaucrat relationship) to block its passage or alter the emphasis of the policy before the policy is adopted (by selecting and withholding information, strategic bargaining with the government and lobbying politicians) or after its adoption (by non-co-operation).

### 3. THE PERCEPTION OF NEED FOR A POLICY

The debate over the establishment of BNOC suggests that BNOC was not intended to be a means to an end but more likely, an end in itself. Policy decisions are concerned with the choice of a strategy that can adapt to a continually changing environment.<sup>9</sup> In the highly uncertain and volatile world oil market of the 1970s the ability of government to adapt to an unstable world situation was a particular policy concern. It has been largely because of this concern that government planning in the offshore oil sector has been institutional and pragmatic - which has itself added to uncertainties. The following sections of the paper are not directly concerned with whether BNOC was, or is, an "effective" organization. Rather the concern is whether any such organization is able, within the democratic framework of the UK, to provide a positive contribution to the offshore oil sector in a manner that is not overwhelmingly political.

The Labour Government's 1974 White Paper on energy policy<sup>10</sup> was produced, significantly, only after the North Sea had become a major political issue. The preceding decade was characterized by the relative freedom from government intervention in the oil industry. The 1973-4 world oil "crisis", the discovery of sizeable oilfields in the North Sea in the early 1970s and the publication of the Committee on Public Accounts (PAC) Report (which was highly critical of the oil tax system), had the effect of pushing North Sea oil to the centre of the political stage. The Department of Energy itself was established in 1974 at least partly as a result of these pressures.

Individuals became aware of the economic potential of North Sea oil. As the cost of acquiring information to the individual diminished (because of the extensive media attention) and individuals' desire for information increased; their coercion threshold was lowered. The combination of these factors meant that it was in the interests of the political parties to formulate oil policies which would maximize votes. As North Sea oil became increasingly politically sensitive, there was an increase in the potential political gains of being seen to be taking action in the oil sector. The perception of dependence for oil on OPEC and the perception of "excess" profits accruing to, mainly foreign owned, oil multi-nationals were prime areas where government action could result in political gain.

As stated earlier, it is the nature of the democratic system in the UK that shields politicians from citizens' preferences. However, once there is a perceived need for, in this case, a domestic oil policy, then in the formulation of that policy other factors become important. These factors include bureaucratic interests, intra-party rivalry, inter-party competition, inter-departmental competition and the activities of various pressure groups and lobby groups.

Labour Government pronouncements and proposals concerning the establishment and rôle of BNOC made in 1974 and 1975 can be seen as part of a bargaining process between groups within the oil policy process. Initial Labour Government intentions were for a 51% participation in North Sea oil based on a "carried interest" system. The "carried interest" proposal was for a voluntary 51% participation with BNOC paying for past and future expenditure on a 51% basis. It is unlikely that 51% participation was ever considered by the government as a rigid requirement. If the straightforward 'socialist' action of 51% participation as originally proposed was implemented by the government there would not only be considerable opposition from the oil industry but also political opposition in Parliament and in the country. Although the government would remain in office it would run the risk of

adverse and embarrassing political publicity and would allow the Opposition to adopt a more popular policy and capture votes. As governments are unsure of voter preferences, the government is keen to minimize risk and take a safe policy option, whilst at the same time it must placate minority groups within its own party by political rhetoric.

A major function of BNOC was to enhance the government's access to, and ability to interpret, oilfield information. Mr Benn, then Secretary of State for Energy, justified the need for active and large-scale participation on the grounds that first-hand experience is vital to gain the necessary expertise and information in all North Sea oil activities.<sup>11</sup> The Labour Government saw its rôle in the North Sea oil sector as one of controlling rather than regulating the industry. It is thus necessary for the controlling system to be able to steer the controlled system using various instruments and techniques. It follows that the controlling body must have more information and expertise than the system to be controlled. If this is not the case, there is a danger that the rôles will be reversed and it is BNOC which steers government policy.

In the process of adopting a policy Niskanen argues<sup>12</sup> that bureaucrats favour economic planning because the influence, and budget size, of the Department increase. Much of the justification for BNOC does not stand up to the criticism levelled at it unless it is accepted that the "national interest" criterion can be achieved by government intervention. The two Downsian assumptions with regard to the motivation of politicians suggest that politicians do not attempt to impose policies that are in the "national interest", however defined, unless the policy is also in direct accordance with the politician's self-interest. The Labour Government's view in 1975 was that state intervention and control in the North Sea was, by definition, in the national interest because it was a socialist action.

One of the functions of BNOC, in common with many other European NOCs, was to forward the 'good' of the whole country.<sup>13</sup> The inescapable consequence of such a wide framework of reference was that BNOC was prevented from taking decisions on purely financial and commercial criteria.

The Conservative Opposition and oil industry pressure groups argued that the bureaucracy involved in BNOC, the expense, the extensive personal powers of the Energy Secretary and the extent of BNOC's rôle in the North Sea were unnecessary. Patrick Jenkin, then Shadow Energy Secretary, criticized BNOC for attempting to be both "like an investment holding company - passive, watchful, steering, monitoring and supervising" and an "active, entrepreneurial body which would aim to compete fairly with existing companies."<sup>14</sup>

From the outset, there seemed to be a conflict between BNOC's activities as a competitive, commercial oil company and as a partner of the private companies gathering confidential information and with an intimate relationship with the government.

#### 4. BNOC 1976-9

The passage through Parliament of the Petroleum and Submarine Pipelines Act<sup>15</sup> which established BNOC on January 1, 1976 was relatively trouble-free. The Act was consistent with Labour Party ideology, there was strong popular support for the government to be seen to be taking some action in the oil sector and the Act increased the stature of the Department of Energy. The combination of these factors resulted in Conservative and oil company objections to the Act being relatively ineffectual.

The creation of BNOC was a major political event and BNOC was explicitly designed to have an especially close relationship with the government, more so than other UK public enterprises. BNOC's relationship with the government was a relationship with both a government department and with government politicians. For

simplicity, it is assumed that the sponsoring organization is a homogeneous body. Within this sponsoring body, although individual civil servants may spend a considerable amount of time dealing with the affairs of BNOC, the higher level civil servants (like politicians) have numerous functions to perform and have many other areas that need their attention. Employees of BNOC however, work full-time in the interests of themselves and BNOC. This argument is not as forceful as in Niskanen's model where the politician is a part-time overseer of a department's activities. In 1977 the Department of Energy was reported to have forty-one officers of principal level and above involved in North Sea oil and BNOC matters.<sup>16</sup> Nevertheless, the relationship can still be viewed as similar to Niskanen's model - a bi-lateral monopoly with BNOC having access to considerably more expertise and information than does the government. If the government is viewed as comprising bureaucrats and politicians then although the government bureaucrat is able to acquire information, and has a stronger relative incentive to do so than the politician, BNOC is in a very strong position with regard to the information it passes to civil servants. However, even then the department may attempt to withhold information from the politician if it is in the department's interests to do so.

The financial structuring of BNOC gave it the opportunity to acquire state funds with the Energy Secretary's consent or to borrow from commercial banks. Obviously BNOC was initially dependent on the government for cash but the government was keen to support BNOC and was sympathetic to its demands. Negotiations were carried out in a favourable atmosphere as the government wanted BNOC to establish itself quickly alongside the oil companies already active in the North Sea.

Thus the relationship between BNOC and the government can be seen in terms of Niskanen-type sponsor/bureaucracy relationship, but with significant differences. The most important difference is that with respect to BNOC and the government, the sponsor cannot be viewed as a homogeneous entity with one set of characteristics

and objectives. Of less importance is that BNOC was able to seek finance from any source. BNOC could only negotiate for commercial loans once it had proved its credibility as an oil company. Thus BNOC was totally dependent on the government and government policy for funds in the first two years of its existence.

The government could not be viewed as a totally passive sponsor as accountability over BNOC was exercised through the National Oil Account (NOA). Two points are significant here. First, the Energy Secretary had extensive personal powers with respect to BNOC's finances. Second, without privileged access to royalty monies in the NOA, BNOC would have had to borrow from the National Loans Fund and would have been subject to conventional parliamentary control. Without the NOA, the government would still have the ability to acquire some knowledge of the operations of BNOC via the PAC and through the Department of Energy, and this would act as a constraint on BNOC's activities. Determining the efficiency of a public enterprise like BNOC is extremely difficult. The wide framework of reference imposed on BNOC makes financial or commercial comparisons unsuitable. A profitable public corporation is a valuable political asset for a Labour Government. If BNOC was seen to be making a sizeable contribution to government revenue it might tend not to be scrutinized as closely as if it had been losing money.

Niskanen assumes the bureaucrat to be a rational utilitarian who, because of the nature of the sponsor/bureaucracy relationship, attempts to maximize the size of his budget. Assuming a rational utilitarian manager in BNOC, his maximand would probably not have been to maximize the size of budget received from the government because other factors in the manager's utility function would not necessarily have increased as BNOC's budget increased. More importantly, other factors in the manager's utility function are likely to have had a higher ranking than did budget size. Increasing its size and growth rate were prime concerns of BNOC but it was the way this was to be achieved and the implications of



alternative methods of financing that are important in the context of this paper.

BNOC was a product of Labour Party doctrine and its structure reflected the Labour Party's belief in the need for Central Government to influence the economy. The Conservatives have consistently opposed the principle of a NOC and stated that they would dismantle the Corporation when they came to power. Thus BNOC executives were concerned with the survival of BNOC and the security of their jobs in the face of substantial political uncertainty. Furthermore, with the exception of political appointees at Board level, BNOC executives and managers would have had similar ambitions to those in private sector oil companies and would have had a natural aversion to the socio-political duties imposed on them by government. It is therefore the assertion here that once BNOC had consolidated its position as a credible oil company it became rational for BNOC executives to seek managerial independence. Managers within BNOC were able to pursue this objective, and were motivated to do so, because of the characteristics of BNOC's relationship with the government.

An important technique by which BNOC could acquire managerial independence was by becoming financially independent. In 1977 an \$825 million loan from commercial banks gave BNOC a degree of independence from the government and at the same time was an added complication to any future Conservative effort to dismantle BNOC.

A second technique was a trend towards the multinationalization of BNOC. This diminished the opportunity for government intervention and it added to the complexities any future break-up of BNOC.

Relaxing the assumption of a homogeneous sponsor, the government may be viewed as comprising civil servants (bureaucrats) and politicians whose ambitions often contradict each other and cause conflicts and distortions. Now, the BNOC executive's need for decision-making freedom is more apparent. Macro-political objectives of senior politicians may conflict with the long term

commercial aims of BNOC. If the government had been the sole financier of BNOC and the Corporation needed to request funds for an investment project the money could be denied because it conflicted with wider government objectives, and not because of the commercial viability of the proposal. Because the Petroleum and Submarine Pipelines Act laid down the institutional potential for further government action and gave the Energy Secretary considerable discretionary powers, political uncertainty resulted.

Rivalry between government departments (most noticeably between the Department of Energy and the Treasury) can lead to bureaucrats making decisions on the basis of whether they are losing some of their duties to another department. If the Treasury has greater influence over government policy than the Department of Energy it may attempt to steer policy in such a manner that Treasury objectives overwhelm the considerations of other Departments. BNOC, in seeking financial independence, was implicitly assuming that political interference (rather than regulation or control), and the added uncertainties this created, was likely to increase over time and may at some stage force BNOC out of existence or reduce its size and power.

##### 5. THE 1979 CONSERVATIVE GOVERNMENT

At the beginning of 1979 the Conservatives were publicizing their plans for the future of BNOC, a future which would have reduced significantly BNOC's influence in the UK oil industry. This led to a great deal of speculation and uncertainty in the offshore oil sector. The complexities of the financial structure of BNOC, the substantial efforts made by Lord Kearton (the first Chairman of BNOC) to make it as difficult as possible to break-up the Corporation and the new 'appreciation' of the value of BNOC revenue to the incoming Administration, resulted in government procrastination and ambiguity with respect to BNOC.

The Conservatives entered Office pledged to decreased state intervention in the economy, and specifically to dismantle BNOC.

In the summer of 1979 the Energy Secretary (David Howell) was facing considerable political embarrassment in that a major oil producing country was suffering petrol shortages. Using BNOC as the instrument by which the government would attempt to divert oil supplies - whilst at the same time considering how to dismantle BNOC - would add to the embarrassment of a staunchly non-interventionist government.

The pressure to make use of BNOC for political purposes would come from some members of the Conservative Party and government who would want BNOC revenue to be used for priority economic purposes (for instance, to help finance government borrowing). These pressures would involve, for example, the Energy Minister having to be prepared to subordinate his own personal and departmental objectives to those of the government as a whole or to those of another department. A Minister would not necessarily be averse to this if it were the case that by being seen to be a loyal government member, his standing and prospects are enhanced in the eyes of the party leader or the party in general. This argument can be extended to include top-level civil servants. It would be the case that senior government bureaucrats and ministers may be prepared to accept a budget reduction (the opposite of Niskanen's thesis) if it were in their personal interests so to do. Less senior bureaucrats would not necessarily have the opportunity to display loyalty and solidarity, and be rewarded for it. These bureaucrats may therefore attempt to change the policy or prevent its effective passage. Thus although senior bureaucrats and ministers may be able to increase their standing by reducing their departmental budget, bureaucratic pressures from within the department may oppose this.

Important sources of opposition to the Conservative Government's plans to dismantle BNOC were from BNOC itself and from the supporters of the Corporation in Parliament. As previously stated, the primary objective of BNOC between 1976 and 1979 was to ensure its long term survival by seeking managerial independence.

After the election of the Conservatives in 1979 a further tactic employed by BNOC was to make itself indispensable to the government, as a source of revenue and as an instrument of policy.

The idea of completely dismantling BNOC was abandoned and various forms of re-structuring and privatizing BNOC were suggested by the government. The Conservative Administration did remove some of the privileges BNOC enjoyed under the previous Labour Government but BNOC was not opposed to this. The privileges had already achieved their purpose in that BNOC was able to borrow on the financial markets, a reflection of its status as an oil company. As a result of the changes BNOC would be almost on an equal footing with private sector oil companies. In addition, because some changes were inevitable, BNOC's compliance would create goodwill with the government. Although BNOC lost its requirement to advise the government on oil matters, there remained a close liaison between BNOC and the Department of Energy.

In the autumn of 1981 David Howell was replaced by Nigel Lawson as Secretary of State for Energy. A major priority for Mr Lawson was the denationalization of BNOC. The delay in dealing with BNOC was causing increasing embarrassment to the government, especially as privatization was central to Conservative ideology. Furthermore, the short term burden of BNOC's proposed expenditure plans (£2000 million by 1986),<sup>17</sup> would, at least partly, have to be met by the Treasury. Thus the government was keen for BNOC to acquire private sector financing.

Philip Shelbourne, appointed Chairman of BNOC in 1980, was strongly in favour of privatizing BNOC. Thus with the zeal of Mr Lawson backed by the Prime Minister, the Treasury and Mr Shelbourne, new impetus was given to the plans for privatizing BNOC. The "Oil and Gas (Enterprise) Act, 1982"<sup>18</sup> provided powers for the government to split BNOC's upstream activities into a subsidiary company which would then be sold, in part, to the public. Ownership of the exploration and production company, Britoil, was transferred to the Secretary of State for Energy on

November 1, 1982. On November 10, 51% of Britoil's issued share capital was offered for sale on the Stock Exchange. In December 1982 Britoil became a private sector oil company with a government shareholding of 49%.

BNOC remained solely as an oil trading company with functions to "secure and dispose of UKCS petroleum in a way which contributes to national security of supply,..... to ensure that the UK economy receives the maximum benefits from the Corporation's access to such petroleum..... and to act as the Government's agent in the sale of oil taken as royalty-in-kind".<sup>19</sup> Thus the government retained considerable and direct influence in the UK offshore oil sector, largely because of the political value of such influence. BNOC's practical use was soon to be emphasised in the political arena following OPEC's London Meeting in March 1983. The British Government was able, through BNOC, to price North Sea oil at such a level as tacitly to support the OPEC pricing agreement and prevent OPEC members, (specifically Nigeria) from attempting to undermine the oil price deal.

Although Britoil was free from uncertain political and bureaucratic interference, the government retained certain powers within the company. As long as the government shareholding in Britoil is greater than 20%, the Energy Secretary is empowered to appoint two Directors to the Board of Britoil. In addition, the government is in possession of the special "golden" share which may be used to control any change in ownership of Britoil. The special share is designed to prevent ownership of Britoil passing to foreign interests.

The delay in the privatization of BNOC illustrates how oil policy intentions can be deflected by political considerations. The privatization programme was central to Conservative policy and the privatization of BNOC was an important political symbol of the government's commitment to free enterprise. Mr Lawson was able to achieve considerable personal repute in the Conservative Government by implementing the privatization policy. Following

the Conservative's General Election win in June 1983, Mr Lawson was promoted to become Chancellor of the Exchequer.

It is important to note a "ratchet effect" of government policy with respect to the privatization of BNOC. The Conservative Government retained a 49% shareholding in Britoil as well as the special powers associated with the "golden" share. In addition, the government ensured it had the potential for extensive control through its ownership of BNOC, now only an oil trading company. The Conservatives were unable, or more likely unwilling, to restore the initial policy situation with regard to participation (i.e. the situation existing prior to the 1974 Labour Administration) with no direct involvement in the UK offshore oil industry.

## 6. CONCLUSION

In examining UK government's oil participation policy since 1974 it is apparent that there are many imperfections which influence the policy process. Casual observation reveals that if in order to achieve an economically efficient allocation of resources the political party has to undertake a vote-losing action, it is unlikely for that action to be taken. Even if a vote-losing policy is implemented, the policy is subjected to various pressures and influences within the policy process and it is likely that the final policy which is implemented will be significantly different from the one originally advocated.

A policy developed as a response to public perceptions of a "crisis" and argued for as being in the "national interest" may achieve the objective of vote maximization. However, as crises pass and public perceptions change politicians and bureaucrats in government retain substantial powers. A policy, whilst satisfying political and bureaucratic ambitions, may have little to do with promoting economic efficiency. It is not suggested that economic efficiency should always take precedence over all other considerations. Nevertheless, if a politician or political party

favours, say, an ideological objective over an objective of economic efficiency, then it is vital for governments to make known the economic costs and implications of the policy in order that preferences of voters may be revealed through the democratic system.

In highlighting the existence and sources of bureaucratic and political pressures in the policy process with respect to oil participation policy, deficiencies of government policies may be identified. In recognizing the government policy process as imperfect the case for the government intervening in the offshore oil industry, in order to improve on situations arising from an imperfect industry, becomes less clear. That the policy process is imperfect results from the assumptions of rational utilitarian individuals in government made in the economic theories of bureaucracies and politicians. It seems naive to assume that as soon as an individual moves from organized market activities to some kind of government position he "shifts his psychological and moral gears"<sup>20</sup> and becomes an altruist.

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