4 HQ

ECGD

18 DEC 1986

cc WP
J Mole

File Saudi Tornados

Export Credits Guarantee Department
PO Box 272
Export House
50 Ludgate Hill
London EC4M 7AY

Telephone 01 382 7000
Direct 01 382
Fax 01 382 7649
Telex 883601
Ans Back ECGD HQ G

Your reference

Our reference

Date 18th December 1986

T J D Downing Esq
Bank of England
Threadneedle Street
LONDON EC2R 8AH

SAUDI ARABIA; YAMAMAH PROJECT

Now that we have received Ministerial authority to offer cover on the lines proposed by Mr Channon to the Chancellor on 11 December (in a letter virtually exactly the same as the draft you saw) I am writing to answer the points raised in your letter of 8 December to Peter Mountfield. These points though important in themselves were considered to be of too technical a nature to be included in the Ministerial correspondence.

First concerning delivery of oil. The Oil Agreement provides for oil to be delivered to Shell/BP fob at an Arabian Gulf VLCC port or fob YANBU, making use of the oil pipe-line, or by means of a Saudi vessel to a Shell/BP facility outside Saudi Arabia. Using this as a base and assuming that any other Oil Agreement will have similar provisions we are defining in our guarantee the term "delivery" as meaning either delivery fob Saudi or Arabian Gulf Port or delivery by discharge into a facility outside the control of KSA.

If Shell/BP cannot send its ships into the Gulf because of war or a blockade and if oil cannot be delivered at any other port because of pipeline capacity constraints and if KSA were not able to ship the oil to a Shell/BP facility and then KSA failed to pay by other means, ECGD would be liable.

You also raised the question of the difference in meaning between "delivery" and "offer for delivery". Whilst it is our intention to cover failure by the Saudis to offer oil for delivery and not failure by Shell/BP to take delivery (other than by reason of the force majeure events described above), we have a practical and legal problem in defining "offer for delivery". We are overcoming this difficulty by talking only about "delivery" (as defined above) but specifically excluding events that we are not prepared to cover (eg default by Shell/BP).

Finally, concerning the points raised in the penultimate paragraph of your letter, I should explain that the number of barrels per day will not directly affect ECGD's maximum liability. This will be set at the outset at $1.6bn and will relate to a quasi-linear amortisation of the $1bn facility (plus interest) over 5 years. The volume of oil agreed between MODUK and MODA may, by agreement between those parties, be changed as may the actual deliveries of oil whether over or under the agreed figure but none of this will change our stated maximum liability. Any such changes will of course affect the operation of our guarantee in the following ways:

a If the volume of oil changes in the agreement between MODUK and MODA, then any failure by the Saudis to deliver will relate to the new volume. Incidentally this is a point that is worrying the banks and I believe they will seek an undertaking from MODUK not to decrease the presently agreed levels (300,000 bpd) without their agreement.

b The actual amounts we pay (within our maximum liability) and the timing of our payments could change.

I hope this letter, necessarily complicated because of the complex nature of the questions you raised, clarifies these issues.

Yours sincerely

P HENLEY