

Title: Cost recovery for consents issued under petroleum or offshore methane gas and carbon dioxide storage licences and Pipeline Works Authorisations. IA No: DECC0095 Lead department or agency: DECC Other departments or agencies: None	Impact Assessment (IA)			
	Date: 19/09/2011			
	Stage: Consultation			
	Source of intervention: Domestic			
	Type of measure: Secondary legislation			
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Summary: Intervention and Options	RPC: GREEN
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Cost of Preferred (or more likely) Option				
Total Net Present Value	Business Net Present Value	Net cost to business per year (EANCB in 2009 prices)	In scope of One-In, One-Out?	Measure qualifies as
-£0.62m	-£3.19m	£0.34m	Yes	IN

What is the problem under consideration? Why is government intervention necessary?
 DECC does not currently charge Industry for consents (such as permission to drill wells) issued under petroleum licences, offshore methane gas licences and carbon dioxide storage licences or for Pipeline Works Authorisations (which allow the construction of offshore pipelines). The cost associated with issuing these consents is therefore not currently felt by those who benefit directly from them. Cost recovery, from introducing a fees and charges regime, would give better price signals and improve resource allocation.

What are the policy objectives and the intended effects?
 To improve resource allocation by making those enjoying these services bear their costs. In addition, charging industry a fee for providing these functions rather than them being subsidised by the taxpayer should allow the maintenance of these services within satisfactory timescales in the face of future constraints on public expenditure allocations.

What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)
Do nothing: Central Government continues to fund the cost of DECC providing the consenting regime. This option will expose DECC to constrained public expenditure allocations in the future and therefore jeopardise DECC's service quality to industry.
Option 1: Introduce charges to (just) cover the Department's costs. Only services with identifiable direct beneficiaries have been selected for inclusion in the scope of the proposed fees and charges regime.
Option 1 is the preferred option. There would be a net benefit to the Exchequer from charging for rather than subsidising services of benefit to a specific part of the upstream oil and gas industry. The charges would not be passed on to consumers. In addition, industry funding the services will mean that they can be sustained to industry's advantage even with future public expenditure constraints. These benefits are thought to justify the relatively small overall resource cost from industry and DECC processing the new fees.

Will the policy be reviewed? It will be reviewed. If applicable, set review date: 01 / 2018					
Does implementation go beyond minimum EU requirements?			No		
Are any of these organisations in scope? If Micros not exempted set out reason in Evidence Base.	Micro Yes	< 20 Yes	Small Yes	Medium Yes	Large Yes
What is the CO2 equivalent change in greenhouse gas emissions? (Million tonnes CO2 equivalent)			Traded: None		Non-traded: None

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible Minister: _____ Date: _____

Summary: Analysis & Evidence

Policy Option 1

Description: Introduce a fees and charges regime for certain upstream oil and gas consents and permits

FULL ECONOMIC ASSESSMENT

Price Base Year 2012	PV Base Year 2012	Time Period Years 10	Net Benefit (Present Value (PV)) (£m)		
			Low: Optional	High: Optional	Best Estimate: -0.62

COSTS (£m)	Total Transition (Constant Price) Years		Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	Optional	0	Optional	Optional
High	Optional		Optional	Optional
Best Estimate	0		0.38	3.19

Description and scale of key monetised costs by 'main affected groups'

The gross fees of around £1.1 million a year (2012 prices) fees would be paid by the upstream oil and gas industry but, after tax relief, the net cost to industry would fall to around £400,000 a year. This includes the net cost to industry of the costs associated with processing the fees.

Other key non-monetised costs by 'main affected groups'

None.

BENEFITS (£m)	Total Transition (Constant Price) Years		Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	Optional	0	Optional	Optional
High	Optional		Optional	Optional
Best Estimate	0		0.31	2.57

Description and scale of key monetised benefits by 'main affected groups'

The beneficiary of the fees would be the Exchequer, though the benefit would be reduced because of the high tax rates applying to profits from upstream oil and gas activities, tax relief on industry's costs associated with processing the fees and a small cost of collecting the fees.

Other key non-monetised benefits by 'main affected groups'

DECC's ability to provide the services that would be charged for would not be constrained by future budget restrictions.

Key assumptions/sensitivities/risks

Discount rate (%)

3.5

The assessment relies on estimates of the numbers of consents of different types which are inherently uncertain. The average effective rate of tax relief is also uncertain but 65% is thought to be a reasonable estimate.

BUSINESS ASSESSMENT (Option 1)

Direct impact on business (Equivalent Annual) £m:			In scope of OIOO?	Measure qualifies as
Costs: 0.34	Benefits: 0	Net: -0.34	Yes	IN

Evidence Base (for summary sheets)

- **Problem under consideration**

DECC does not currently charge Industry for consents (such as permission to drill wells) issued under petroleum licences, offshore methane gas licences and carbon dioxide storage licences or for Pipeline Works Authorisations (which allow the construction of offshore pipelines). The cost associated with issuing these consents is therefore not currently felt by those who benefit directly from them.

- **Rationale for intervention**

To improve resource allocation by making those enjoying these services bear their costs. As set out in *Managing Public Money* (http://www.hm-treasury.gov.uk/psr_mpm_index.htm), it is Government policy to charge for many publicly provided goods and services. Charging for services relieves the general taxpayer of costs properly borne by users who benefit directly from a service. This allows for a more equitable distribution of public resources and enables lower public expenditure and borrowing. No attempt has been made here to apply a shadow price to Exchequer income to reflect the reduced deadweight cost from consequently lower taxation.

Charging helps allocate use of goods or services in a rational way because it prevents waste through excessive or badly targeted consumption. It also makes for easier comparisons with the private sector, promotes competition and helps develop markets. The norm is to charge at full cost. None of the exceptions set out in *Managing Public Money* (Box 6.1) applies to the services under consideration here.

There is a specific power to charge for such services in section 188(1) of the Energy Act 2004. This provides a power to make charges in relation to the Secretary of State's "relevant energy functions". Section 188(1)(a) refers to "services or facilities provided or made available by him in the carrying out of his relevant energy functions". This is scoped to cover staff and overhead costs involved in administering consents. Furthermore, section 188(1)(d)(ii) allows charges to be made "for purposes which are incidental to, or otherwise connected with, the carrying out of any of those functions". These powers thus allow costs associated with the maintenance of the online UK Oil Portal to be recovered provided those costs are attributable to the Secretary of State's relevant energy functions.

In addition, charging industry a fee for providing these functions rather than them being subsidised by the taxpayer should allow the maintenance of these services within satisfactory timescales in the face of future constraints on public expenditure allocations.

- **Policy objective**

The aim of introducing a full cost recovery charging regime for the consents/activities described below is to relieve the burden on the taxpayer of providing these services by ensuring that those directly benefitting from them pay for them; they will thereby contribute equitably to the cost of their own regulation. It is intended that this will be achieved by transferring the (pre-tax) costs of providing these services from the general taxpayer to the users of the service. This should improve resource allocation by making those enjoying these services bear their costs. In addition, charging industry a fee for providing these functions rather than them being subsidised by the taxpayer should allow the maintenance of an effective service to industry within satisfactory timescales in the face of future constraints on public expenditure allocations.

The consents or activities that DECC (with the agreement of the Treasury) considers suitable for the new charges are:

- Field Development Plan approvals and Gas Storage Plan Development Plan approvals; these consents allow the licence holder to construct the oil and gas production and storage infrastructure to an approved design
- Drilling consents (including exploration, appraisal and development wells)

- Pipeline Works Authorisations (which allow the construction of offshore pipelines)
- Production, flaring and venting consents (allowing oil and gas to be produced at agreed rates or gas to be safely flared or vented to the atmosphere where the gas is otherwise not at economic rates to warrant being piped to shore)
- Licence assignments (the transfer of an interest in a licence from one company to another)
- Carbon Dioxide "Storage Permit" approvals; these permits allow the injection of carbon dioxide into geological features for the purpose of climate change mitigation (as opposed to purely for the purpose of enhanced oil recovery where no such Storage Permit is required)

- **Description of options considered**

Do nothing

Under this option, Central Government would continue to fund the cost of DECC providing the consenting regime. This option would expose DECC to constrained public expenditure allocations in the future and therefore jeopardise its service to industry.

Option 1: Introduce Charges (and keep the gross income, with no consequent reduction in DECC budgets which have already been set assuming these charges are introduced)

Charge a fee for consents under petroleum licences, offshore methane gas and carbon dioxide storage licences. In light of current economic conditions and the recent Government Spending Review it is essential that DECC recovers costs wherever possible. This would seem a reasonable approach given that a fee should not be an unreasonable burden on industry and that the Offshore Environment Unit of DECC already charges a fee for processing offshore (oil and gas) environmental permits and consents. This option would also enable the Department to continue providing an effective service to Industry. Beyond the very small costs for Government and industry of administering the charges regime, it is not expected there will be any transitional costs or annual recurring costs to society as a whole if the preferred option is adopted.

- **Monetised and non-monetised costs and benefits of each option (including administrative burden)**

Based on the analysis below, the estimated gross cost of the proposed fees is around £1.0 million a year (2012 prices). In addition, those paying the fees would incur some cost associated with making the necessary payments to DECC. Based on discussions on hourly administration costs with a small sample of operators, these are estimated at an average of £50 per consent ; in practice, there may be some scope for payments to be grouped, reducing the average cost somewhat. The consultation exercise for the new regime will ask business for more information so this administrative burden on them can be quantified more fully.

With an estimated 1,300 or so consents a year being charged for, the total gross cost to industry would be of the order of £1.1 million a year. But the upstream industry faces a special tax regime on its profits from oil and gas production which means that after tax it bears only 19 to 38 per cent of the gross cost; for details of the regime, see <http://og.decc.gov.uk/en/olgs/cms/explorationpro/taxation/taxation.aspx>. Assuming that most of the activities relate to new fields, the average tax rate would be nearer 62 per cent than 81 per cent. If it were 65 per cent, which is thought to be a reasonable central estimate, the post-tax cost to industry of the proposed charges would average £0.4 million a year (2012 prices).

An assumption has been made that the administration of the invoicing regime will be absorbed by an existing DECC employee (at Administrative Officer level) and that this will take up about a quarter of his/her time. This equates, with all-in staff cost and Departmental overhead taken into account, as an annual (opportunity) cost to the Department of some £11,000. The pay cost is taken from a real time pay report for the officer concerned and the Departmental Overhead was provided by the Department's Finance Unit.

- **Rationale and evidence that justify the level of analysis used in the IA (proportionality approach)**

The rationale for charging for a service benefitting a specific group is straightforward. The cost associated with issuing consents is not currently felt by those who benefit directly from them. Cost recovery, from introducing a fees and charges regime, would give better price signals and improve resource allocation. We have therefore adopted a light-touch approach to the assessment of resulting costs and benefits, making reasonable central assumptions. These demonstrate a small overall resource cost. That cost is very small in the context of the costs of the activities being consented. We know that cost-reflective fees will vary over time, as the complexity of the activities being consented varies, and that the number of activities being consented to will also change. But, in the absence of specific pointers to the likely changes, we have assumed that activity and fees will be constant (at estimated 2012 levels) for the 10 year horizon considered here.

- **Risks and assumptions**

The main assumptions underlying this assessment relate to the variable pattern of demand for the services for which a charge is proposed. The intensity of all of these activities can go up or down from year to year, sometimes significantly. This means that it is difficult to be sure how much the charges will raise and it will be impossible to guarantee costs are (just) fully covered in any one year. The table below uses estimated average fully-allocated costs and best estimates of the number of consents a year of each type. The types of consent are those for which different average costs are expected. In some cases they reflect the location of the team undertaking the work, with higher staff and accommodation costs for the London-based team which covers the SNS (Southern North Sea), IS (Irish Sea) and onshore than the Aberdeen-based team which covers the WoS (West of Shetland), NNS (Northern North Sea) and CNS (Central North Sea).

	Proposed Fee (£)	Average Number/ Year	Total Cost/Income (£000)
Censents for New Wells	647	100	64.7
Consents for Sidetracks/Suspensions	532	50	26.6
Consents for Recompletions/Re-entries	506	50	25.3
Licence Assignments without operator consideration	909	200	181.8
Licence Assignments with operator consideration	1,538	50	76.9
WoS, NNS & CNS Field Development Plans (FDPs)	16,500	13	214.5
SNS & IS FDPs	10,500	6	63.0
WoS, NNS & CNS Production Consents	622	120	74.6
SNS & IS Production Consents	792	50	39.6
Onshore Production Consents	400	20	8.0
WoS, NNS & CNS Flare Consents	530	130	68.9
SNS & IS Flare Consents	432	1	0.4
Onshore Flare Consents	240	20	4.8
WoS, NNS & CNS Vent Consents	530	40	21.2
SNS Vent Consents	392	100	39.2
Onshore Vent Consents	40	20	0.8
New Pipeline Works Authorisations	2,500	21	52.5
PWA Variations/Deposit Consents	200	255	51.0
PON 6 Approvals	920	20	18.4
Estimated Total Income from Fees (£000)		1,266	1,032.3

The larger fees above (e.g. for FDPs) are averages. In practice, a day rate would be estimated and the fee per FDP consent would reflect the actual number of days' effort related to that consent.

DECC has no experience of consenting to Gas Storage Plan Development Plans or approving Carbon Dioxide Storage Permits and the number of such consents/approvals is likely to be very low, at least for the foreseeable future, so they are not included in the above analysis.

- **Direct costs and benefits to business calculations (following OIOO methodology)**

There are no direct monetary benefits to industry but industry should benefit from DECC's ability to provide the services that would be charged for not being constrained by future budget restrictions. The costs to business follow from the gross costs to be recovered, the average rate of tax relief (assumed to be 65% as explained above) and the increase in industry's costs required to process the fees (net of tax relief).

It is not anticipated that the imposition of charges at the sort of level suggested would affect the level of upstream activity resulting in a change in demand for any of the consents. Similarly, it is not expected that the level and scale of charges proposed would be passed on to final consumers of oil or gas.

There will be a small administrative burden on industry in complying with the regime. The consultation exercise for the new regime will gather evidence on this administrative burden so it can be quantified more fully for the purposes of One In One Out.

- **Summary and preferred option with description of implementation plan**

Option 1 is the preferred Option. It would be fairer because the cost associated with issuing consents would be felt by those who benefit directly from them and it would also give better price signals and improve resource allocation. Reducing the call on general taxation should reduce its deadweight cost (by an unquantified amount). In addition the industry funding the services will mean that they can be sustained to their advantage far into the future even with public expenditure constraints.

Subject to consultation and Ministerial decision, it is proposed that the new charges would be brought into effect from the start of financial year of 2013/14. Any consent subject to the new charging regime submitted for approval after 1 April 2013 will therefore be subject to the payment of the appropriate fee.

Businesses of all sizes can participate in UK upstream (exploration and production) oil and gas activities but, except for a few onshore licensees, micro-businesses are not likely to be affected as they lack the requisite resources. Those micro-businesses that choose to participate expect to face the same cost conditions as other upstream licensees so there is no reason to exempt them from the proposed charging regime. The charges are, anyway, extremely small by comparison with their other costs (and income) from upstream activities.

Specific impact tests/Wider Impacts

Carbon Impact Assessment

These proposals will not have an effect on any of the determinants of carbon emissions such as the level or energy-intensity of production.

Competition assessment

This standard competition assessment test involves considering whether the proposal directly limits the number or range of suppliers, indirectly limits the number or range of suppliers, limits the ability of suppliers to compete or reduces suppliers' incentives to compete vigorously. The proposals will not affect competition in any of these ways.

Small Firms impact test

The costs of the proposals are not expected to fall disproportionately on small businesses.

Unintended consequences

Consideration has been given to potential adverse side effects of the proposals and none has been identified to date.

Legal Aid Impact Test & Justice System

The impacts of the legal aid test are not relevant to the introduction of a fee in relation to consents pertaining to petroleum licences or offshore methane gas and carbon dioxide storage licences or for Pipeline Works Authorisations issued under Part III of the Petroleum Act 1998.

Economic

No specific economic effects are expected beyond those in the core analysis.

Other environmental effects

The proposals are not expected to have any effect on environmental outcomes.

Health Impact Assessment

There are no health impacts as a consequence of the proposals.

Sustainable Development Principles

These proposals directly supports one of the five principles of sustainable development – that of 'promoting good governance'.

Other equality issues

The following reports the conclusions made for the other issues that have been considered to test for differential impacts:

Rural areas and regional. The proposal will affect companies who submit a request for a consent or pipeline works authorisation. Therefore this will depend on where these companies are based.

Devolved countries. The proposals apply to Great Britain, all of UK territorial waters and to the United Kingdom Continental Shelf.

Race equality. None identified

Gender equality. None identified

Disability equality. None identified

Human rights. None identified

Age and income. None identified.

Annex 1: Post Implementation Review (PIR) Plan

A PIR should be undertaken, usually three to five years after implementation of the policy, but exceptionally a longer period may be more appropriate. A PIR should examine the extent to which the implemented regulations have achieved their objectives, assess their costs and benefits and identify whether they are having any unintended consequences. Please set out the PIR Plan as detailed below. If there is no plan to do a PIR please provide reasons below.

Basis of the review:

DECC will review the policy after five years and will also review the charges on a yearly basis as a matter of good practice. The Regulations are likely to provide for fees to be determined on an annual basis. If the level of fees changes as a result of this determination, any changes will be reported to the Treasury.

Review objective:

To ensure the charging mechanism is operating efficiently and the new measures are working as expected and to inform the level of charges.

Review approach and rationale:

The focus is likely to be reviewing and monitoring the charging mechanism and evaluating whether the system is achieving the intended objective.

Baseline:

The baseline position is continuing with the current system whereby central government continues to fund the Licensing, Exploration and Development Branch within DECC.

Success criteria:

This will be developed by DECC to ensure the Department recovers its costs and carries out its functions pertaining to petroleum licences or offshore methane gas and carbon dioxide storage licences or for Pipeline Works Authorisations issued under Part III of the Petroleum Act 1998. Full cost recovery will allow the Department to maintain those functions to Industry.

Monitoring information arrangements:

DECC will develop systems to review and monitor information to ensure full cost recovery.

Reasons for not planning a PIR:

N/A