Regulatory Policy Committee	**Validation of the One-in, Two-out Status and the Net Direct Impact on Business**
Validation Impact Assessment (IA)	Underground Access Rights clauses in 2014 Infrastructure Bill – impact on oil and gas activities
Lead Department/Agency	Department for Energy and Climate Change
IA Number	DECC 0177
Origin	Domestic
Expected date of implementation	SNR 9
Date of Regulatory Triage Confirmation	27 March 2014
Date submitted to RPC	22 September 2014
Date of RPC Validation	30 October 2014
RPC reference	RPC14-FT-DECC-2054(2)
Departmental Assessment	
One-in, Two-out status	OUT
Estimate of the Equivalent Annual Net Cost to Business (EANCB)	-£65.09 million
RPC assessment	**VALIDATED**

Summary RPC comments

The validation IA is fit for purpose. The proposal reduces regulatory barriers to the development of shale gas, resulting in increased production and, therefore, net benefits to business. Based upon the information provided, the Committee is able to validate the estimated equivalent net benefit to business of £65.09 million each year. The Department should take account of the Committee's comments before publishing the IA.

Background (extracts from IA)

What is the problem under consideration? Why is government intervention necessary?

"Although the Crown owns the mineral rights to oil and gas in Great Britain,

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operators wishing to extract oil and gas have to negotiate with landowners for underground access rights. This is a time consuming, uncertain and potentially costly process. The operator can refer the case to the court to establish whether compulsory acquisition of rights should be granted. This process is likely to take between 1 and 2 years, creating further delays, uncertainty and additional costs to developers. Developers of deep geothermal energy projects face similar issues with regard to underground access rights but have no recourse to the court. The Infrastructure Bill measures would apply equally to underground access for oil and gas exploration/production and deep geothermal. Deep geothermal is considered in a parallel impact assessment."

What are the policy objectives and the intended effects?

"To simplify the existing procedure for underground access, whilst ensuring that key features, such as payment and notification, are retained. Nothing in the proposed measures will have any effect on other regulatory or legal provisions including the licencing [sic] regime (petroleum or water abstraction), planning permission, health and safety regulation and environmental regulation. As noted above, a parallel impact assessment considers the impact on deep geothermal energy projects of the proposed changes to underground access rights."

RPC comments

The Department's proposal is to grant businesses underground access (below 300 metres) for the exploration and/or extraction of oil and gas. (Access to deep geothermal energy is subject to a separate validation.) This access will be accompanied by a "voluntary payment" from these businesses. The preferred option is for this to be a "community payment" rather than payments to individual landowners, which would be more costly to administer and negotiate. The proposal includes a reserve power to introduce "payment in statute" if industry reneges on the voluntary agreement. Overall, the Department expects the proposal to reduce barriers to oil and gas exploration, provide investors with greater certainty around investment decisions, and thereby facilitate exploration and extraction of oil and gas earlier and at a higher level.

Benefits

The IA estimates the benefits to business as the surplus of revenue over costs from the additional activity that would take place. The key assumptions that affect the calculations are: activity levels (the number of shale gas pads); production levels (number of wells and average recovery per well); development and production costs; gas prices; and time profile. The assumptions here use official DECC forecasts (e.g. for gas prices) and information provided by industry (e.g. for development and production costs).

The Department estimates that the effect of the proposal will be to increase

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steadily the number of new shale gas pads, rising to an additional four per year by 2023, before falling back thereafter. The assessment of likely production levels is informed by the Department's estimates of shale gas reserves and advice from industry, which is in turn informed by its experience in North America. The Department acknowledges the high degree of uncertainty, but states that it uses a "*relatively conservative set of assumptions*" (page 8). This is supported by the assumptions on production levels used being below those in the recent reports by the Institute of Directors and Ernst & Young.

The method and data used to estimate benefits are in line with that used in the recent Model Clauses IA, assessed as fit for purpose by the Committee in June 2014. The baseline for the present IA incorporates the anticipated benefits from the model clauses proposal. There is, therefore, no double counting of benefits. This addresses a comment in the RPC's validation statement on model clauses.

<u>Costs</u>

The IA includes an estimated £25,000 per year for the cost per project/site to business of administering the compensation payment. This has been informed by discussions with industry. The calculations exclude the cost of the payment itself, which is treated as a transfer.

It would appear that taking a "reserve power" to introduce payment in statute, if industry reneges on the agreement, means that the compensation payment is not truly voluntary. This appears to be accepted by the Department through its inclusion, in calculating the direct costs to business, of the administrative cost of the payment. The treatment of the payment as a transfer is only correct for the calculation of the direct costs to business if the transfer is between businesses and/or civil society organisations.

At the Committee's request, the Department has provided additional information on this issue. This information confirms that these payments are likely to be relatively small. (The current proposal is for a one-off payment of around £20,000 per well. In the IA, each project is modelled as having 12 wells.) Moreover, the payment is expected to be to a community body for community benefit. This in line with the industry's existing community benefits scheme. On the basis that the payment is likely to be relatively small and a transfer between businesses and/or civil society organisations, the Committee accepts that the exclusion of the payment will not significantly affect the EANCB. The impact assessment should, however, address this issue more directly, incorporating the information provided separately to the Committee.

Based upon the IA and the supporting cost model (which was provided, on request, separately to the RPC), the Committee can validate the estimated net savings to business of £65.09 million each year.

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Additional points

The IA would benefit from a greater explanation of the “reserve power”, which could lead to the introduction of the payment in statute if industry reneged on the “voluntary” agreement. Information provided separately by the Department states that this would involve passing secondary legislation, with its own consultation and IA. In reviewing any such IA, the Committee would expect to see the assumptions regarding community payments revisited and any direct impact on business scored for OITO purposes.

The IA would also benefit from including some further information on the points below, even though they do not affect validation of the EANCB.

- a summary table of costs and benefits over time, from the cost model. This would help readers to understand further how the Department estimates the overall costs and benefits;

- better discussion of the environmental effects and public risk, as this is a matter of wide public interest.

Signed		**Michael Gibbons,** Chairman

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