Summary: Intervention & Options

Department /Agency: **Department for Transport**	**Title:** **Impact Assessment of the proposal to bring PILOT into line with actual training costs**	
Stage: Consultation	**Version: 1**	**Date:** 04 March 2010
Related Publications: Consultation on bringing PILOT into line with actual training costs		

Available to view or download at:

http://webarchive.nationalarchives.gov.uk/+/http://www.dft.gov.uk/consultations/closed/2010-21/

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

The tonnage tax training requirement was introduced in 2000. This intervention was deemed necessary to give registered firms a tax base which allowed them to compete effectively internationally. As part of the tonnage tax regime a requirement was introduced that companies recruit and train officer trainees or make a payment in lieu of training (PILOT). This was designed to correct perceived market failure in the maritime labour market, manifest in declining numbers of officers and associated impacts on sectors employing officers and former seafarers. In order to encourage companies to train, rather than to pay PILOT, it was always the intention that PILOT rates should be broadly in line with actual training costs. Although uprated annually in line with inflation, PILOT rates have failed to keep pace with actual training costs; it is therefore necessary to take steps to try to ensure that they remain in line in the future.

What are the policy objectives and the intended effects?

The objective is to bring PILOT rates more closely into line with actual training costs. The intended effect is that companies will be encouraged to recruit officer trainees rather than to pay PILOT. This should further the policy objective, which is to increase the number of UK officer trainees. The eventual ultimate aim is to increase the number of newly qualified UK officers to a level at which they replace those who leave the industry.

What policy options have been considered? Please justify any preferred option.

Option 1: <u>Do Nothing</u>. This would potentially mean that the extent to which training costs exceed PILOT rates would widen over time, causing an increasing disincentive for companies to train rather than to pay PILOT.

Option 2: <u>Take action to bring PILOT levels into line with actual training costs, and make provision for a regular review of PILOT rates against those actual costs</u>. The preferred option as it would incentivise tonnage tax companies, where possible, to provide training rather than to make PILOT payments.

When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects? The policy would be reviewed at the same time as the PILOT rates themselves. PILOT rates would only be raised in line with actual training costs.

<u>Ministerial Sign-off</u> For consultation stage Impact Assessments:

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:

Paul Clark

....Date: 17 March 2010

Summary: Analysis & Evidence

Policy Option: 2	**Description: Take action to bring PILOT levels into line with actual training costs, and make provision for a regular review of PILOT rates against those actual costs.**

	ANNUAL COSTS		
COSTS	**One-off** (Transition) **Yr**	Description and scale of **key monetised costs** by 'main affected groups' 1.) There will be an additional cost to firms that currently pay PILOT. Assuming these firms continue to pay PILOT and 3,000-4,500 PILOT payments per year, the increase in the value of PILOT payments has been estimated at approximately £0.13-0.19 million in 2010/11 and £0.25-£0.38 million p.a. from 2011/12. However, the increase in the value of PILOT payments will be lower (and could potentially be negative) if these firms decide to train more officers.	
	£ 0		
	Average Annual Cost (excluding one-off)		
	£ 0.2-0.4 million	**Total Cost** (PV)	**£ 2.0 – 3.1 million**
	Other **key non-monetised costs** by 'main affected groups' 1.) If firms that currently pay PILOT choose to train more officers instead of paying PILOT, they will incur the costs of training these officers instead. However, the total cost of Option 2 to these firms is not expected to exceed the Total Cost (PV) identified above. 2.) As noted above, if the number of PILOT payments significantly declines, the impact on the value of PILOT payments received by the Maritime Training Trust could potentially be negative.		

	ANNUAL BENEFITS		
BENEFITS	**One-off** **Yr**	Description and scale of **key monetised benefits** by 'main affected groups' 1.) The value of PILOT payments received by the Maritime Training Trust could increase. Assuming 3,000-4,500 PILOT payments per year, the increase in the value of PILOT payments has been estimated at approximately £0.13-0.19 million in 2010/11 and £0.25-£0.38 million p.a. from 2011/12. However, the increase in the value of PILOT payments will be lower (and could potentially be negative) if the firms currently paying PILOT decide to train more officers.	
	£		
	Average Annual Benefit (excluding one-off)		
	£ 0.2-0.4 million	**Total Benefit** (PV)	**£ 2.0 – 3.1 million**
	Other **key non-monetised benefits** by 'main affected groups' 1.) The incentive to train officers rather than pay PILOT is likely to be increased, which could cause some firms that currently pay PILOT to choose to train more officers instead of paying PILOT. 2.) There could be longer term benefits for the maritime labour market. 3.) There could be benefits for the maritime training industry and related industries.		

Key Assumptions/Sensitivities/Risks 1.) The monetised costs and benefits shown above are estimated on the basis that firms currently paying PILOT continue to pay PILOT. Should an increase in PILOT result in more firms choosing to train officers, the estimated monetised costs and benefits would both be reduced. 2.) The level of PILOT payments per year, and consequently the monetised costs and benefits, is uncertain. 3.) The Net Benefit below only reflects the monetised costs and benefits identified in this impact assessment.

Price Base	Time Period	**Net Benefit Range** (NPV)	**NET BENEFIT** (NPV Best estimate)
Year 2008	Years 10	**£ 0**	**£ 0**

What is the geographic coverage of the policy/option?			UK	
On what date will the policy be implemented?			1 October 2010	
Which organisation(s) will enforce the policy?			DfT	
What is the total annual cost of enforcement for these organisations?			£ N/A	
Does enforcement comply with Hampton principles?			Yes	
Will implementation go beyond minimum EU requirements?			N/A	
What is the value of the proposed offsetting measure per year?			£ N/A	
What is the value of changes in greenhouse gas emissions?			£ N/A	
Will the proposal have a significant impact on competition?			No	
Annual cost (£-£) per organisation (excluding one-off)	Micro	Small	Medium	Large
Are any of these organisations exempt?	No	No	N/A	N/A

Impact on Admin Burdens Baseline (2005 Prices)			(Increase - Decrease)
Increase of £ 0	Decrease of £ 0	**Net Impact**	**£** 0

Key: **Annual costs and benefits: Constant Prices** **(Net) Present Value**

Evidence Base (for summary sheets)

1. Background

Since 2000, shipping companies have been able to either opt into tonnage tax or to remain in normal corporation tax. A key feature of the tonnage tax is the minimum training obligation (MTO). The MTO in respect of officers is for a company to recruit, and train one officer trainee each year for every 15 officer posts in its fleet.

Companies which can show good reasons why they are unable to recruit or sponsor trainees may instead be permitted to make payments in lieu of training (PILOT). PILOT payments may also arise where there is a shortfall in the training which the company should have provided, or where there is an incremental training commitment as a result of additional vessels joining the fleet.

The Maritime Training Trust (MTT) is the industry body which has been established to collect PILOT payments. It uses the funds raised from the PILOT scheme to promote merchant navy training. The purpose of this spending is to raise awareness about the benefits of a career at sea, and possible subsequent job opportunities.

When the tonnage tax was introduced in 2000, the intention was that the PILOT payment level should be at least equivalent, or slightly more, than the cost of training a trainee, to encourage companies to provide actual training. Since then, PILOT rates have been uprated annually in line with the Treasury GDP deflator, but the MTT are concerned that the PILOT rate has now fallen significantly below actual training costs.

After reviewing the costs of training to both company employers and other training providers, the MTT have proposed that PILOT should be increased in line with actual training costs, that this increase should be staged over two years, and that there should be a regular review of PILOT, say every two years, to ensure that it continues to be in line with actual training costs.

2. Why is Government Intervention required?

Lord Alexander of Weedon conducted an Independent Enquiry into a Tonnage Tax[1] in 1999, which recommended a minimum training obligation as an eligibility condition for entry into the tonnage tax regime. The tonnage tax was introduced in 2000, and, as part of the tonnage tax regime, a requirement was introduced that companies recruit and train officer trainees or make PILOT payments. This was designed to correct a perceived market failure in the maritime labour market, manifest in declining numbers of officers, and associated impacts on sectors employing officers and former seafarers. In the late 1990's, merchant navy officer cadet intake was around 400 a year, whereas an intake of approximately 1,200 was needed in order to maintain the number of officers at sea and those employed in shore-based maritime-related sectors of the economy[2].

In order to ensure that the scheme operates as intended, further Government Intervention is now considered to be necessary in order to ensure that PILOT rates are equivalent to the cost of training an officer.

3. Options

3.1 Option 1: Do Nothing. The potential effect of this would be that the extent to which training costs exceed PILOT rates could widen over time if officer training costs continue to rise faster

[1] http://www.hm-treasury.gov.uk/ent_ee_tonnage.htm
[2] *UK's Requirements for People with Experience of Working at Sea*, The University of Wales, 1996.

than the level of general price inflation, causing an increasing disincentive for companies to train rather than to pay PILOT. This is the counterfactual for the purposes of this impact assessment.

3.2 Option 2: Bring PILOT levels into line with actual training costs, and make provision for a regular review of PILOT rates against those actual costs. This is the preferred option as it would incentivise tonnage tax companies, where possible, to provide training rather than to make PILOT payments.

After reviewing the costs of training to both company employers and other training providers, the MTT have proposed that:

1. PILOT should be increased in line with actual training costs;
2. The increase should be staged over two years; and
3. There should be a regular review of PILOT, say every two years, to ensure that it continues to be in line with actual training costs.

The proposed changes to PILOT, and the costs and benefits of Option 2, are presented in Section 4 below.

4. Analysis of the costs and benefits of Option 2

4.1 Groups and sector affected

The proposals will potentially affect all companies or groups within the tonnage tax regime. However, companies and groups will only be affected to the extent that they meet their training obligation by paying PILOT rather than by training or sponsoring actual trainees. Companies who meet the whole of their training obligation through the provision of actual training will be unaffected. As paying PILOT was never meant to be a cheaper option than providing actual training, it is considered that the proposals will be fair to all companies within tonnage tax.

Assuming that an increase in the level of PILOT would not influence participation within the tonnage tax regime, there are two possible responses from shipping companies that participate in the tonnage tax regime to an increase in the level of PILOT:

1. If companies currently paying PILOT continue to pay PILOT then there would be a transfer of resources from shipping companies to the MTT. This would constitute a transfer payment as no good or service is received in return. The value of the transfer would be equal to the increase in the level of PILOT compared to the counterfactual case.

2. If companies currently paying PILOT switch and begin to train officers, then there would be a transfer of resources from shipping companies *and* the MTT to officer training providers. This includes a reduction in transfer payments compared to the counterfactual (equal to current PILOT) and a cost increase to shipping companies within the tonnage tax, which would be equal to the difference between current PILOT levels and the actual training provision chosen. This cost has not been estimated in this impact assessment, but it is expected that this would be similar to the value of the transfer in 1, as the intention is that PILOT would be adjusted to reflect the actual cost of officer training.

4.2 Costs of Option 2

4.2.1.Cost to Firms Continuing to Pay PILOT

The PILOT fee is expressed in pounds (£) per trainee month. It is made up of a 'basic' rate, plus an additional element (roughly another 10%, rounded to the nearest £) in respect of the MTT's overhead costs.

Taking the 2008/09 'basic' rate of PILOT of £610 as the baseline, the MTT have proposed that the 'basic' rate of PILOT should be raised to £694 per trainee month at 2008 prices (plus 10% in respect of the MTT's overhead costs), and that this increase should be staged over two years. The MTT proposal is based on a review of the cost of officer training courses, both to company employers and to other training providers. DfT has obtained quotes directly from several training providers, in the context of which it is satisfied that the MTT's estimates appear to be reasonable.

The actual PILOT rate for 2008/09 is shown in Table 1 below. The actual PILOT rate for 2009/10 was set at £623 (£610 in 2008 prices), having been increased in line with the treasury GDP deflator. Real PILOT rates for 2010/11 and 2011/12 showing the proposed increases for those years are also shown. All values are shown in real 2008 prices.

Table 1 – Current & Proposed PILOT Rates (£ 2008)

Year	2008/09 (Actual PILOT rate) £ 2008	2009/10 (Actual PILOT rate £ 2008	2010/11 (projected) £ 2008	2011/12 (projected) £ 2008
Current PILOT levels (Option 1) per month				
Basic Rate	£610	£610	£610	£610
Overhead costs	£ 61	£ 61	£ 61	£ 61
Total pilot per trainee month	£671	£671	£671	£671
MTT Proposed Increases in PILOT (Option 2) per month				
Basic Rate	£610	£610	£652	£694
Overhead costs	£ 61	£ 61	£ 65	£ 69
Total pilot per trainee month	£671	£671	£717	£763

The increase in PILOT from the baseline year of 2008/09 to 2010/11 would therefore be £46 per trainee month, before taking inflation into account, and the projected increase between 2010/11 and 2011/12 would also be £46 per trainee month, again before taking inflation into account. The overall impact of the proposed PILOT rates is to increase them by £92 per trainee month between 2008/09 and 2011/12, again before taking inflation into account. For the purposes of this impact assessment, it is assumed that the level of PILOT would remain at this level in future years in 2008 prices.

The number of PILOT payments between 2000/01 and 2008/09 is presented in Table 2 below.

Table 2 – Number of PILOT Payments (2000/01 to 2008/09)[3]

	Number of Trainee Months	Number of PILOT Payments
2000/01	862	186
2001/02	4,689	1,142
2002/03	9,590	1,657
2003/04	13,043	2,457
2004/05	15,612	3,293
2005/06	16,549	4,066
2006/07	17,648	4,410
2007/08	18,805	3,021
2008/09*	20,596	2,683

The number of PILOT payments in a given year is uncertain. Therefore, in order to estimate the value of this cost over the 10-year appraisal period, it is necessary to make a number of assumptions about the number of PILOT payments that would be made each year. Firstly, it is assumed that the increase in the level of PILOT would not influence behaviour of firms. Secondly, on the basis of the number of pilot payments in recent years, it is thus assumed that

[3] *Incomplete Data

the number of PILOT payments would be between 3,000 and 4,500 per year in the 10-year appraisal period.

On the basis of the above assumptions, the increase in the level PILOT has been estimated to result in an additional cost to the shipping industry of approximately £0.13-0.19 million in 2010/2011 and approximately £0.25-£0.38 million per year from 2011/2012. The appraisal period is 10 years. Over the 10-year appraisal period, the present value of the additional cost to the shipping industry has been estimated at around £2.0-3.1 million.

4.2.2 Cost to Firms Switching to Training Officers Instead of Paying PILOT

Alternatively, shipping companies that are currently paying PILOT could choose to switch to training officers in the face of increases in PILOT. In this case, they would incur additional costs equal to the difference between current PILOT levels and the costs of the chosen training provision. Given that PILOT is being revised to reflect the actual cost of training, the cost increase is likely to be similar under both options, but would in the this case be expected to be *no more* than the increase in the level of PILOT.

4.3 Benefits of Option 2

The main benefit of Option 2 is that companies would face a greater incentive, where possible, to provide actual training rather than to pay PILOT. The longer term benefits thus relate to the potential to increase the number of officers in training. This could have wider benefits to society if it helps to address the perceived market failure in the maritime labour market, and helps to ensure a stock of trained sea-farers for the UK's various shipping businesses.

Alternatively, if firms choose to pay the increased level of PILOT fees, then the MTT would have more funds to spend on the promotion of seafarer training. In the long run, this is likely to have similar, albeit lesser benefits, to the case discussed above in terms of helping to correct the maritime labour market failure.

In both cases, there could also be benefits to the maritime training industry and related industries.

5. Specific Impact Tests

5.1 Competition Impact Assessment

It is considered that bringing PILOT into line with actual training costs would be unlikely to have a significant impact on competition. Companies, to the extent that they pay PILOT rather than carry out actual training, may face an increase in costs. However, it was never the policy intention that PILOT should be a cheaper or easier option than providing actual training, and companies opting into the tonnage tax would not have expected this to be the case.

5.2 Small Firms Impact Test

The minimum tonnage tax training requirement is calculated in proportion to the number of officer posts in a company's fleet. It is considered that this ensures that the burden on any firms would be proportionate to the size of the operation and would avoid placing an undue burden on any small firms. In addition, it is considered that the types of companies operating ships internationally and operating under the tonnage tax regime are unlikely to qualify as small firms.

5.3 Race, Gender and Disability Equality

It is considered that there are no race, gender or disability equality impacts to these proposals.

Specific Impact Tests: Checklist

Type of testing undertaken	***Results in Evidence Base?***	***Results annexed?***
Competition Assessment	Yes	No
Small Firms Impact Test	Yes	No
Legal Aid	N/A	N/A
Sustainable Development	N/A	N/A
Carbon Assessment	N/A	N/A
Other Environment	N/A	N/A
Health Impact Assessment	N/A	N/A
Race Equality	Yes	No
Disability Equality	Yes	No
Gender Equality	Yes	No
Human Rights	N/A	N/A
Rural Proofing	N/A	N/A