Title: UKCS Environmental Regulations: Fees and Charges **IA No:** DECC0186 **Lead department or agency:** Department of Energy and Climate Change (DECC) **Other departments or agencies:** None	Impact Assessment (IA) **Date:** 6/05/15 **Stage: Final** **Source of intervention:** Domestic **Type of measure:** Secondary legislation **Contact for enquiries:** Richard Brooks Richard.brooks@decc.gsi.gov.uk

Summary: Intervention and Options

RPC: Opinion Status - Green

Cost of Preferred (or more likely) Option				
Total Net Present Value	**Business Net Present Value**	**Net cost to business per year**	**In scope of One-In, One-Out?**	**Measure qualifies as**
-£0.05m	-£12.1m	£1.0m	No	Zero Net Cost

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

DECC has recently undertaken a review of the current fee charging schemes for the environmental regulation of the offshore oil and gas industry. The purpose of the review was to assess whether existing arrangements were compliant with guidelines on *Managing Public Money* and to identify whether new fee schemes were required in order to recover future costs associated with delivering services under other new or amended regulations. The review's findings have identified that secondary legislation is required in order to recover the costs of services delivered by DECC to industry that had previously been raised ultra-vires i.e. without the necessary legal authority. In addition, secondary legislation is also required to recover the cost of delivering services under two new / amended Regulations. In the absence of intervention, the cost associated with DECC providing regulatory services to industry would be met by the taxpayer, rather than those companies which directly benefit from the activities undertaken.

What are the policy objectives and the intended effects?

The policy objective is to ensure that the costs of environmental regulatory services which are provided by DECC to oil and gas operators are fully recovered from industry. Through the introduction of secondary legislation, the government will have powers to recover costs associated with providing regulatory activities that have previously been raised ultra-vires. In addition, fee charging schemes will also be created for new / amended Regulations in order that costs incurred in the future can be recovered. The measures will relieve the burden on the taxpayer and ensure that those companies directly benefiting from the services pay for them, which should also improve resource allocation.

What policy options have been considered, including any alternatives to regulation?

Two main policy options have been considered:

- **Option 1:** The 'do nothing' option would constitute a continuation of current arrangements under which central government would fund the cost of regulatory functions from general taxation. This approach was ruled out as it would not achieve the policy objective.
- **Option 2:** Introduce secondary legislation that ensures DECC has the necessary powers in place to recover its costs through fee charging schemes. This is the preferred option as it will ensure companies directly benefiting from regulatory services meet the cost associated with their provision.

Will the policy be reviewed? It will be reviewed. **If applicable, set review date: 2018**					
Does implementation go beyond minimum EU requirements?			N/A		
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:** N/A	**Non-traded:** N/A	

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 2

Description: Introduce fee charging schemes via secondary legislation to recover the costs of regulatory activities from industry.

FULL ECONOMIC ASSESSMENT

Price Base Year: 2015	PV Base Year: 2015	Time Period Years: 10	Net Benefit (Present Value (PV)) (£m)		
			Low: -£0.04m	**High: -£0.05m**	**Best Estimate: -£0.05m**

COSTS (£m)	**Total Transition** (Constant Price)	Years	**Average Annual** (excl. Transition) (Constant Price)	**Total Cost** (Present Value)
Low	n/a	n/a	£0.005m	**£0.04m**
High	n/a		£0.006m	**£0.05m**
Best Estimate	**n/a**		£0.006m	**£0.05m**

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

The fee schemes will recover the costs associated with DECC providing regulatory services to oil and gas operators. This imposes a new cost on business (estimated at £12.1m in a central case, with a range of £10.9m to £13.3m), but at societal level reflects a transfer from the taxpayer to business. There will also be a small additional annual cost to business and society overall reflecting the need for oil and gas operators to process invoices and pay fees to DECC. This is the only identified cost of the measure at societal level.

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

All significant costs arising from the proposal have been monetised. The cost to government of administering the fees scheme and issuing invoices to industry is included in the estimated cost to be recovered from industry annually. The additional administrative cost to government / society from these activities relative to the baseline will be minimal and therefore have not been identified separately in line with the principle of proportionality.

BENEFITS (£m)	**Total Transition** (Constant Price)	Years	**Average Annual** (excl. Transition) (Constant Price)	**Total Benefit** (Present Value)
Low	n/a	n/a	n/a	n/a
High	n/a		n/a	n/a
Best Estimate	**Nil**		**Nil**	**Nil**

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

There are no monetised benefits from the proposal. The introduction of fee schemes will not affect the level or quality of regulatory activities undertaken by DECC on behalf of the oil and gas industry.

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

The proposal will ensure that the costs of environmental regulatory services provided by DECC to the oil and gas operators are fully recovered from industry. The measures will therefore relieve the burden on the taxpayer and ensure that those companies directly benefiting from the services pay for them, which should also improve resource allocation.

Key assumptions/sensitivities/risks	Discount rate: 3.5%

- The NPV base year is 2015 and all values are expressed in 2015 prices. A real discount rate of 3.5% has been used with costs assessed over an appraisal period of 10 years (2015-2024).
- It is assumed that fees and administrative costs will first be incurred in 2015 and then remain constant in real terms annually over the appraisal period of 10 years.
- Estimated costs to DECC which are the basis of fees charged to industry are based on historical outturn costs and forecast cost in the future.
- Administrative costs for industry are calculated based on the estimated time required to process invoices and hourly wage data which is considered representative of the employees likely to undertake the activity. Further detail is provided in the assumptions section.

BUSINESS ASSESSMENT (Option 2)

Direct impact on business (Equivalent Annual) £m:			**In scope of OITO?**	**Measure qualifies as**
Costs: £1.0m	**Benefits: Zero**	**Net: -£1.0m**	No	Zero Net Cost

Evidence Base

1. Problem under consideration

1. The Offshore Oil and Gas Environment and Decommissioning Unit (OGED) in the Department of Energy and Climate Change (DECC) has recently undertaken a review of the current fee schemes for the environmental regulation of the offshore oil and gas industry. The purpose of the review was to assess whether the existing schemes are compliant with HMT guidelines on *Managing Public Money*[1] and to identify whether additional fee schemes were required as a result of the transposition of the EU Offshore Safety Directive and the amendments to the Fluorinated Greenhouse Gases Regulations.

2. Through a number of fee charging schemes, DECC currently recovers the direct costs incurred in the processing and administration of permits issued and the associated monitoring and compliance activities to operators in relation to the environmental regulation of the UK Continental Shelf (UKCS). The fee payable by oil and gas operators reflects the actual departmental resource costs of processing, evaluating, issuing and administrating the permits within DECC. In recent years, around £9 million per annum in fees has been recovered in total from industry.

3. Following the conclusion of the review, there are two key findings:

   a. Of the c.£9 million recovered from industry in previous years via fees, there are services provided by DECC - under five sets of environmental Regulations (a-e in Table 1 below) - for which fees of around £1.4 million per annum were being charged that did not have the requisite cover under secondary legislation. These fees have therefore been raised *ultra vires*, meaning that they have previously been charged without the necessary legal authority.

   b. Services to be provided to industry in relation to two other Regulations - The Fluorinated Greenhouse Gases Regulations (amended) 2015 and The Offshore Installations (Offshore Safety Directive) (Safety Case etc.) Regulations 2015 (f-g in Table 1 below) – require fee provisions in order that costs can be recovered in the future.

Table 1: Regulations for which legislation is required to create a fees scheme

a.	The Offshore Petroleum Production and Pipe-lines (Assessment of Environmental Effects) Regulations 1999 (as amended),
b	The Offshore Petroleum Activities (Conservation of Habitats) Regulations 2001 (as amended),
c.	The Offshore Marine Conservation (Natural Habitats, &c) Regulations 2007 (as amended),
d.	The Merchant Shipping (Oil Pollution Preparedness, Response and Co-operation Convention) Regulations 1998.
e.	The Marine and Coastal Access Act 2009
f.	The Fluorinated Greenhouse Gases Regulations (amended) 2015
g.	The Offshore Installation (Safety Case) Regulations 2015

4. There are sufficient fee raising powers in primary legislation to make the regulations and address the current gap in legislative cover, in relation to both the new and the more long-standing regulations. DECC therefore intends to introduce secondary legislation in order for the Department to have the appropriate legislative powers in place to recover from industry via fees, the costs associated with

[1] HM Treasury (2013) Managing Public Money 2013 [web], available at: https://www.gov.uk/government/publications/managing-public-money.

providing these additional activities, rather than passing the costs onto the taxpayer. The proposed approach is consistent with the guidelines on *Managing Public Money.*

2. Rationale for intervention

5. Secondary legislation is required in order for DECC to establish fee raising powers for activities undertaken on behalf of oil and gas operators on the UK Continental Shelf (UKCS). The legislative powers will enable the Department to recover its resource costs from companies who will benefit from the services provided. There are specific primary legislation powers to provide for fees in relation to the Secretary of State's relevant energy functions under the Regulations in Table 1.

6. The proposed approach is therefore in line with long-established practice and Government policy - as set out in "Managing Public Money"[2] - that Government recovers the costs of the services it provides, where this is possible. In particular it states that: *"This [cost recovery] can be a rational way to allocate resources because it signals to consumers that public services have real economic costs. Charging can thus help prevent waste through badly targeted consumption. It can also make comparisons with private sector services easier, promote competition, develop markets and generally promote financially sound behaviour in the public sector."*

7. The guidance makes clear that charges for services provided by public sector organisations normally pass on the full costs of provision. Charging for services therefore 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.

3. Policy objective

8. The policy objective is to ensure that the costs of environmental regulatory services (as detailed in Table 1 above) which are provided by DECC to the oil and gas industry are fully recovered.

9. Through the introduction of secondary legislation, the government will assume powers to recover the costs associated with five schemes which were previously collected ultra vires. In addition, the government intends to put in place legislation to recover the costs incurred in the future with respect to The Fluorinated Greenhouse Gases Regulations 2015 and The Offshore Installations (Offshore Safety Directive) (Safety Case etc.) Regulations 2015.

10. A full cost recovery charging regime for the activities described above will relieve the burden on the taxpayer of providing these services by ensuring that those directly benefitting from them pay for them; companies will thereby contribute equitably to the cost of their own regulation. It is intended that this will be achieved by transferring the full (pre-tax) costs of providing these services from the general taxpayer to the users of the service. This should improve resource allocation by ensuring that those benefiting from these services bear their costs.

4. Description of options considered

11. Two options were considered:

- **Option 1:** The 'do nothing' option was ruled out on the basis that it would not achieve the policy objectives. This approach would have constituted a continuation of current arrangements under which central government would have to fund the cost of DECC providing the regulatory functions from general taxation.

[2] HM Treasury (2013) Managing Public Money 2013 [web], available at: https://www.gov.uk/government/publications/managing-public-money.

- **Option 2:** Introduce secondary legislation that ensures the Department has the appropriate power in place in order that OGED can recover its costs though fees**.** This is the preferred option as it will ensure that companies directly benefitting from the regulatory services meet the cost associated with their provision. The approach is therefore consistent with the guidelines on *Managing Public Money*. This option will also enable the Department to continue providing an effective service to industry.

5. Monetised costs and benefits

COSTS

Business costs

12. For the purposes of this analysis, the counterfactual for estimating the net additional cost of introducing fees schemes to cover activities undertaken with respect to the Regulations in Table 1 is assumed to be the continuation of the current arrangements. Under current arrangements DECC meets the costs of providing regulatory services which are ultimately funded through general taxation. This approach reflects the fact that DECC ceased recovering costs from industry for these activities in 2014/15 once it became evident that fees had previously been raised ultra-vires. In the absence of the proposed secondary legislation these current arrangements would persist. It should be recognised that the secondary legislation required to introduce the cost recovery schemes will not expand the scope of regulatory activity undertaken by DECC, but rather serves to ensure that companies benefiting from the services bear the costs.

13. The new fees schemes will recover the costs associated with DECC providing these regulatory services to oil and gas operators. As reported in Table 2 below, the cost is estimated at around £1.4 million (2015 prices) in total across six sets of Regulations. Estimates are based on out-turn costs in incurred in 2014/15 for the services which had previously been charged ultra-vires and on departmental forecasts of the costs likely to be incurred for services provided in relation to The Fluorinated Greenhouses Gases Regulations (2015), for which a fee scheme is also being established.

14. While a fee scheme is being established to recover DECC's costs for services provided under the Offshore Safety Directive (OSD, 2015), the costs have not been included within the Impact Assessment (IA). This is because the costs which will be recovered from industry were quantified within the final stage OSD IA and therefore including them again here would result in double counting. This IA relates to the introduction of secondary legislation which will enable the recovery of these costs, but in itself does not expand the regulatory burden which will be implemented via transposition of the OSD. In summary, the costs to DECC to be recovered from industry were previously estimated at around £119,000 (2014 prices) on an average annual basis, with an NPV of around £963,000 over an appraisal period of ten years. (2015 NPV base year).

Table 2: Annual fees payable by business, central estimate (2015 prices)

Regulatory activities	Total cost to be recovered via fees (central estimate)
The Offshore Petroleum Production and Pipe-lines (Assessment of Environmental Effects) Regulations 1999 (as amended)	£245k
The Offshore Petroleum Activities (Conservation of Habitats) Regulations 2001 (as amended)	£288k
The Offshore Marine Conservation (Natural Habitats, &c) Regulations 2007 (as amended)	£190k
The Merchant Shipping (Oil Pollution Preparedness, Response and Co-operation Convention) Regulations 1998	£568k
The Marine and Coastal Access Act 2009	£83k
The Fluorinated Greenhouse Gases Regulations 2015	£24k
The Offshore Installation (Safety Case) regulations	n/a
Estimated costs to be recovered	**£1,397k**

15. It should be recognised that there is uncertainty around the future costs that will be incurred by DECC and subsequently recovered from industry via fees. This is due to the variable pattern of demand for the services for which charges will be introduced. The intensity of all of these activities can go up or down from year to year, but based on historical experience, costs are not expected to vary significantly from the estimated total of around £1.4 million per annum. However, for the purpose of this analysis an indicative range of +/- 10% has been applied to the central estimate to illustrate the potential level of volatility in fees charged to industry as shown in Table 3 below.

Table 3: Estimated annual range of fees, 2015 prices.

	Estimated range of costs to be recovered via fees
Low	£1,257k
Central	£1,397k
High	£1,537k

16. In addition, those companies paying fees will incur administrative costs associated with processing invoices and making the necessary payments to DECC. Across all of the Regulations for which costs will be recovered via fees, based on the current number of operators in scope it is estimated that 40 companies will be charged fees. The intention is for them to be invoiced by DECC on a biannual basis, resulting in 80 invoices being issued in total each year. Based on previous discussions with industry, it is estimated that the processing of invoices should take on average around 0.5 days each, resulting in around 40 days of work for industry as a whole each year.

17. For the purposes of this analysis, the estimated administrative costs to industry associated with processing invoices are based on official statistics for UK mean full time hours per week and median hourly wages, as detailed in the assumptions section below. Annual administrative costs to industry are thereby estimated at **£5,609** based on 40 days (304.8 hours) per annum at an average hourly wage of £18.40 (including superannuation and ENIC costs, 2015 prices).

18. As reported in Table 4 below, the total (fees + admin costs) additional net cost to business in Net Present Value (NPV) terms over the appraisal period of ten years is estimated to be in the range of £10.9 million to £13.3 million, with a central estimate of £12.1 million (2015 prices). The ranges reflect the effect of varying the central assumptions on costs by +/- 10%.

Table 4: Net costs to business, NPV, £ thousands, 2015 prices

	Low	Central	High
Fees	£10,823k	£12,026k	£13,229k
Admin costs	£43k	£48k	£53k
Total	**£10,867k**	**£12,074k**	**£13,282k**

Societal costs

19. As outlined in paragraph 12 above, the introduction of secondary legislation in order to recover DECC's costs from industry will not expand the scope of regulatory activity undertaken with respect to the range of environmental Regulations. The estimated cost to be recovered via fees as shown in Table 4 above is therefore a transfer from the taxpayer to business and does not represent an additional resource cost at societal level. As societal level, the only additional resource cost is the estimated administrative cost to business in processing invoices issued by DECC, which on central assumptions is relatively small at around **£48,000 (NPV, 2015 prices)** over the appraisal period of ten years. We undertake sensitivity analysis on the administrative cost to business in processing invoices issued by DECC of +/- 10%, as highlighted below, leading to a low of £43,000 (NPV, 2015 prices) and a high of £53,000 (NPV, 2015 prices). The cost to government of administering the fees scheme and issuing invoices to industry is included within the estimated cost to be recovered from industry annually and has not been itemised separately. The additional administrative cost to government / society from these activities relative to the baseline would will be minimal (as demonstrated by the central estimate of an annual cost to industry of £5,609 in 2015 prices) and therefore have not been separated quantified in line with the principle of proportionality.

BENEFITS

20. There are no monetised benefits from implementing the proposal. The introduction of fee schemes will not affect the level or quality of regulatory activities undertaken by DECC on behalf of the oil and gas industry. However, the proposal will ensure that the costs of environmental regulatory services provided by DECC to the oil and gas operators are fully recovered from industry. The measures will therefore relieve the burden on the taxpayer and ensure that those companies directly benefiting from the services pay for them, which should also improve resource allocation.

Rationale and evidence that justify the level of analysis used in the IA

21. The analysis contained in this Impact Assessment is considered proportionate to the proposed measure and magnitude of potential costs to business and society as a whole. Estimated costs to DECC are based on a combination of historical experience (for existing regulations) and forecast costs in the future (for relatively new Regulations). It is acknowledged that the annual amount of cost-reflective fees charged to industry will vary over time, as the as the complexity of the activities being regulated varies. An indicative range of +/- 10% on the central estimate has been used to demonstrate the potential annual variance but it is recognised that charges could vary to a greater or lesser extent in line with the regulatory services provided by DECC. Administrative costs are held constant in real terms over the appraisal period which is considered a reasonable assumption. The administrative costs are small in annual and NPV terms relative to the estimated fees payable by industry. The total estimated costs to industry over the appraisal period are also small both in the context of the operating costs of oil and gas companies and in relation to the costs of the activities being permitted through the regulatory activities.

Risks and assumptions

The key assumptions used in the analysis are:

- The NPV base year is 2015 and all values are expressed in 2015 prices. A real discount rate of 3.5% has been used with costs assessed over an appraisal period of 10 years (2015-2024).
- It is assumed that fees will first be charged in 2015 and then remain constant in real terms annually over the appraisal period of 10 years.
- Estimated costs to DECC which are the basis of the assumed fees charged to industry are based on historical outturn costs.
- Administrative costs to business are estimated based on the following assumptions:

- 80 invoices are issued to industry each year, each taking 0.5 days to process, resulting in 40 days of work for industry in total each year.
- Mean weekly full-time paid hours (excluding overtime) of work in the UK in 2014 of 38.1 hours, implying 7.6 hours per day, assuming a working week of 5 days. 40 days' work therefore equates to 304.8 hours[3].
- Salary costs are assumed to be the average of mean hourly earnings (excluding overtime) for the 'admin and secretarial' (£10.81) and 'professional occupations' (£19.38) occupation groups in 2014, which equates to £15.10 per hour[4]. The assumed hourly rate has then been uprated to 2015 prices using the HMT deflator series (31 March 2015) with a further 20% included to reflect employer superannuation and ENIC costs, resulting in an estimated hourly wage cost as used in the calculation of £18.40.
- Total admin costs per annum are thereby calculated as the product of 304.8 hours input per annum and the hourly rate of £18.40, resulting in the estimate of £5,609 per annum. This cost is assumed to be constant in real terms over the appraisal period of ten years.

Direct costs and benefits to business calculations (following OITO methodology)

22. As reported in Table 4 above, the estimated cost to business in NPV terms is £12.1 million (central estimate, 2015 prices) over an appraisal period of ten years. The cost is comprised of fees and administration costs. The resulting Equivalent Annual Net Cost to Business (EANCB) is around £1.0 million (2010 NPV base year, 2009 prices).

23. The policy is however considered out-of-scope of the One-In-Two-Out (OITO) rule under the "Fees and Charges" exemption. The proposal is consistent with government policy to move towards full cost recovery as set out in the Managing Public Money guidance and should therefore be considered as Zero Net Cost.

Wider Impacts

24. 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. Moreover, 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 regulatory activities. Consumers will not be affected by the proposals as the price of oil and gas are set on an international market basis.

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

6. Small and Microbusiness Assessment (SMBA)

26. The exact number of small or microbusinesses (defined as having up to 49 FTE and 10 FTE employees respectively, as per BIS Better Regulation Framework Manual) in the exploration or production of the UKCS is unknown, however, both types of companies operate in this sector. The costs of the proposals are not expected to fall disproportionately on small businesses. 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

[3] ONS, Annual Survey of Hours and Earnings, 2014 Provisional Results, Hours Worked.. http://www.ons.gov.uk/ons/rel/ashe/annual-survey-of-hours-and-earnings/2014-provisional-results/stb-ashe-statistical-bulletin-2014.html#tab-Hours-worked

[4] ONS, Annual Survey of Hours and Earnings, 2014 Provisional Results, Earnings by occupation.. http://www.ons.gov.uk/ons/rel/ashe/annual-survey-of-hours-and-earnings/2014-provisional-results/stb-ashe-statistical-bulletin-2014.html#tab-Earnings-by-occupation

resources. If a small business was to become involved they would only be one of several co-venturers on licensed fields. These co-venturers make an agreement among themselves governing existing and future operations, including the apportionment of operational costs and associated commercial benefits between the parties and none of them would be solely responsible for meeting the full costs of activities related to oil and gas production. Additionally Guidance and support will be available to companies in respect of understanding what compliance looks like and what is required. 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

7. Summary and description of implementation plan

27. Option 2 is the preferred Option. It would be fairer because the cost associated with environmental regulatory activities would be felt by those who benefit directly from them and it would also give better price signals and improve resource allocation. 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.

28. Subject to Ministerial decision, it is proposed that the new charges would be brought into effect from the start of July 2015. Any environmental regulatory activity subject to the new charging regime submitted for approval after 1 July 2015 will therefore be subject to the payment of the appropriate fee.