



House of Commons
Scottish Affairs Committee

**Effects of tax increases
on the oil industry:
Government Response
to the Committee's
First Report of Session
2007–08**

**First Special Report of Session
2007–08**

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The Scottish Affairs Committee

The Scottish Affairs Committee is appointed by the House of Commons to examine the expenditure, administration, and policy of the Scotland Office (including (i) relations with the Scottish Parliament and (ii) administration and expenditure of the office of the Advocate General for Scotland (but excluding individual cases and advice given within government by the Advocate General)).

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The committee is one of the departmental select committees, the powers of which are set out in House of Commons Standing Orders, principally in SO No 152. These are available on the Internet via www.parliament.uk.

Publications

The Reports and evidence of the Committee are published by The Stationery Office by Order of the House. All publications of the Committee (including press notices) are on the Internet at www.parliament.uk/scotaffcom. A list of Reports of the Committee in the present Parliament is at the back of this volume.

Committee staff

The current staff of the Committee are Dr Sue Griffiths (Clerk), Jyoti Chandola (Second Clerk), Duma Langton (Committee Assistant), Karen Watling (Secretary), Becky Crew (Secretary) and Nicola McCoy (Secretary).

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First Special Report

1. The Scottish Affairs Committee published its First Report of Session 2007-08 on 30 November 2007.¹ On 28 January 2008 we received a memorandum from the Scotland Office, which contained a response to the Report. The memorandum is published as an Appendix to this Report.

¹ First Report from the Scottish Affairs Committee, Session 2007-08, *Effects of tax increases on the oil industry*, HC 35

Appendix

This memorandum provides the Government's response to the conclusions and recommendations identified in the Scottish Affairs Committee's report "Effects of tax increases on the oil industry" (HC 35), which was published on 30 November 2007.

Introduction

1. The Government welcomes the Committee's Report and its recommendations, which accord with the Government's own objectives and its commitment to a strong and vibrant UK oil and gas economy. Written evidence from HM Treasury was presented to the Committee for its inquiry and officials from HM Treasury and HM Revenue and Customs also appeared before the Committee on 31 October 2006.

Response to Recommendations and Findings

Recommendation 1

We conclude that it is impossible to isolate with certainty the impact of tax increases from that of other factors such as price or initiatives designed to stimulate investment or increase recovery, including the PILOT programme or the brown field initiatives (paragraph 17).

2. The Government supports this conclusion. However, it should be noted that the Government undertook a considerable amount of analysis before it decided to increase the rate of the supplementary charge from 1 January 2006 and the conclusion of that analysis was that the impact on the industry, on investment and more widely, was likely to be very small indeed.

Recommendation 2

In our view, the fiscal regime is unlikely to be the most important factor driving investment decisions in major fields. Although tax is clearly significant, the nature of the oil and gas fields, the underlying geology and future oil and gas prices are more likely to be the dominant drivers, but the fiscal regime may be a factor affecting investment in older, more marginal fields (paragraph 17).

3. The Government agrees that the underlying geology and future oil and gas prices are the dominant drivers of investment and hence ultimate recovery levels. The Government does, however, have an important role to play in ensuring that the regulatory and fiscal regimes help deliver the best possible future for the UK continental shelf (UKCS).

Recommendation 3

There is a need to balance the return on investment and the return to the UK taxpayer for the use of its natural resource (paragraph 18).

4. The Government has twin objectives for the fiscal regime – to promote investment and production whilst striking the right balance between producers and consumers and ensuring a fair return for the UK taxpayer from our natural resources.

Recommendation 4

We conclude that a simple fiscal regime that is consistent and predictable would be of most benefit to the industry and the UK in the long term (paragraph 22).

5. The Government agrees. It believes that overall the current fiscal regime successfully strikes the right balance referred to above and ensures that producers and consumers benefit appropriately from the production of the UK's oil and gas reserves. The consultation document "Securing a sustainable future: a consultation on the North Sea Fiscal Regime" which the Government published in December 2007 sets out a proposed package of reforms to the fiscal regime that will improve certainty and stability as well as helping to simplify the fiscal regime and reduce administrative burdens.

Recommendation 5

We are heartened by the positive moves by the Treasury to consult on the North Sea fiscal regime and by the engagement of industry with that consultation (paragraph 25).

6. The Government welcomes the Committee's support for its consultation on the North Sea fiscal regime. "Securing a sustainable future" sets out the Government's conclusions on the discussion process with the oil and gas industry and other stakeholders to date, including a proposed package of reforms to the fiscal regime, and will also form the basis for ongoing discussions on outstanding issues.

Recommendation 6

Within the industry, there is clearly a perception of instability and if there are to be further changes to the fiscal regime they should seek to improve stability and predictability, without harming the UK's already competitive position or depriving the UK Government of a fair share in the economic rent from the exploitation of its natural resources. Changes to the fiscal regime should aim to make the system simpler to administer both for companies and HM Revenue and Customs (paragraph 28).

7. The Government has published a set of criteria that it considers it would be desirable any changes to the fiscal regime meet. Any changes should:

- Promote investment and production
- Ensure a fair return for the UK taxpayer
- Be non-distortionary
- Be equitable
- Improve stability
- Be sustainable, and

- Reduce the administrative burden

The proposed package of reforms set out in the December 2007 consultation document was carefully assessed against these criteria. They will help improve stability and provide certainty to investors, as well as simplifying the fiscal regime and reducing the administrative burden it imposes.

Recommendation 7

We urge the Government and the industry to engage constructively in the current dialogue and to build on that dialogue going forward once the current consultation comes to an end (paragraph 29).

8. The Government remains committed to promoting a healthy and prosperous UK oil and gas industry. As part of this commitment, the Government recognises the importance of continued engagement with the oil and gas industry and other stakeholders. Both BERR and HM Treasury Ministers already have regular meetings with industry leaders. We recognise the expertise that those in industry have in this area and believe the best future for the North Sea fiscal regime can be achieved through close co-operation and discussion.

Scotland Office

28 January 2008