House of Commons

Committee of Public Accounts

Public cost of decommissioning oil and gas infrastructure

Eighty-Ninth Report of Session 2017–19

Report, together with formal minutes relating to the report

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The Committee of Public Accounts

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Summary

Significant uncertainty remains about the future costs to taxpayers of decommissioning offshore oil and gas assets. HM Revenue & Customs (HMRC) estimates that oil and gas companies will pass on £24 billion of decommissioning expenditure to taxpayers through tax reliefs, but there remains a wide range of possible future costs as most companies are still improving the certainty of their cost estimates. If oil and gas companies can reduce their decommissioning costs then, in turn, UK taxpayers will benefit through a reduction in the value of tax reliefs that the government provides. The OGA claims to have helped oil and gas companies to reduce the expected cost to decommission their offshore assets by 7%, and we recognise the value it has added by benchmarking performance, making data more widely available and encouraging the sharing of best practice. But the direct impact of the OGA is hard to isolate from other factors influencing company decision-making, particularly the wider economic situation.

There is potential for the UK to become a global leader in decommissioning skills and technology but we are concerned that the Department for Business, Energy and Industrial Strategy (the Department) does not yet have a clear plan for maximising the potential economic benefits. The Department must ensure taxpayers are protected from the risk of footing the bill for decommissioning fracking assets, where there are fewer protections than for offshore oil and gas. The Department also needs to ensure its support for oil and gas remains compatible with its other activities aimed at achieving climate change goals, including ensuring alignment with the development of carbon capture, usage and storage, which could potentially reuse offshore oil and gas assets.

Introduction

The UK's offshore oil and gas reserves are running out. As a result, oil and gas companies are increasingly decommissioning assets that are no longer extracting resources profitably. Decommissioning means plugging and abandoning wells and removing structures, such as platforms, to return the seabed to its natural state as far as possible in accordance with international regulations. Oil and gas companies have spent more than £1 billion on decommissioning in each year since 2014. The OGA expects decommissioning to cost between £45 billion and £77 billion overall, with most expenditure in the next 20 years. HMRC estimates that taxpayers will contribute £24 billion to the cost of decommissioning through tax reliefs. Taxpayers are additionally liable for the cost of decommissioning assets that oil and gas companies cannot afford to decommission themselves. The Department has overall responsibility for the safe, cost-effective and environmentally sensitive decommissioning of offshore oil and gas infrastructure. In 2015, it established the OGA to work with oil and gas companies to reduce the overall cost of decommissioning. The Department also monitors the financial health of oil and gas companies and can require companies to set aside money to pay for future decommissioning if it thinks there is a risk of the bill falling to taxpayers.

Conclusions and recommendations

1. **There is significant uncertainty over the potential costs to taxpayers of decommissioning offshore oil and gas assets.** Future decommissioning costs are uncertain because oil and gas companies are at the early stages of decommissioning and are still learning about how much different activities will cost. The OGA forecasts that the cost of decommissioning to companies will be between £45 billion and £77 billion. HM Revenue and Customs (HMRC) estimates that the cost to taxpayers from tax reliefs associated with decommissioning will be £24 billion based on the central estimate of the OGA's range. But it has not estimated what the costs to taxpayers would be if decommissioning costs are at the top end of the OGA's range. At the same time, oil and gas companies are commissioning new assets in line with the government's objective to maximise recovery of remaining oil and gas reserves. New projects could generate tax revenues for the government but will also add to the total decommissioning bill and increase the future cost of decommissioning to taxpayers.

   Recommendation: ***As part of its next estimate of decommissioning costs, expected in June 2019, the OGA should set out how it is making its estimate more certain and what the expected impact of new and as-yet uncosted projects could be.***

2. **It is unclear how actions taken by the Department and the OGA are reducing decommissioning costs for oil and gas companies.** The Department established the OGA in 2015 to encourage companies to reduce their decommissioning costs. The OGA says it has helped oil and gas companies to achieve a 7% reduction in their expected costs of decommissioning through benchmarking performance, making data more widely available and encouraging the sharing of best practice. The OGA estimates that if companies achieve its target for reducing expected costs by 35% by 2022, UK taxpayers will benefit by £8.6 billion through a reduction in tax reliefs. But it is difficult to isolate the impact of the OGA's activities from wider economic conditions that influence oil and gas companies' decisions. Additionally, the OGA has only published estimates of future costs and has not compared costs already incurred with its previous estimates to demonstrate whether savings have actually been achieved.

   Recommendation: ***The Department and the OGA should set out by July, and report to Parliament annually thereafter, on: the direct impact it has had on reducing decommissioning costs; and the actual decommissioning costs incurred during the previous year set against what the OGA had forecast.***

3. **The Department does not yet have a clear plan to ensure the UK maximises the benefit of developing exportable decommissioning skills and resources.** The UK is one of the first countries in the world to start decommissioning its offshore oil and gas assets on a large scale. This presents an opportunity for the UK to become a global leader in decommissioning skills and technology that can be exported to other regions. The government announced in the 2018 Budget a call for evidence to identify ways the UK can become a global hub for decommissioning. Since then, the UK and Scottish governments (in partnership with Aberdeen University) have helped fund the creation of the National Decommissioning Centre as part of the drive to become a world-leading centre for decommissioning research &

development (R&D). But industries that have been nurtured with UK tax incentives and R&D funding can take intellectual property and move abroad, reducing benefits from taxpayer-funded schemes. We are concerned that the Department does not yet have a clear vision for how the benefits for taxpayers of government support for decommissioning industries will be realised.

Recommendation: ***The Department should set out by July its strategy for maximising the economic benefit of the development and export of decommissioning skills and resources.***

4. **The Department has a worrying lack of understanding of the potential for government liabilities to decommission assets used in fracking.** In offshore oil and gas, the government is ultimately liable to decommission assets that the operating companies cannot afford to decommission themselves. There is some protection given by the fact that partner operators and previous owners of assets are liable before it falls to the government. The Department focuses its monitoring on the 20% of assets which it considers to be highest risk because they have never been owned by one of the largest companies and has required nine companies to set aside £844 million for future decommissioning costs. In contrast, backers of fracking schemes may often be small companies with limited financial resources. The Department tells us that landowners are liable if project backers cannot decommission their assets, but we are concerned that determining liability may not always be as straightforward as the Department believes, and that the liability will ultimately fall to the government. The Department must ensure it sets the terms for how fracking assets are decommissioned before the industry grows further.

Recommendation: ***The Department should write to the Committee by the end of June 2019 explaining the decommissioning arrangements for fracking, including a full and clear explanation of the responsibility for subsequent costs once licences have been returned to the Government, and what it is doing to prevent liabilities falling to taxpayers.***

5. **Government support for oil and gas may become incompatible with its long-term climate change objectives.** As well as providing tax reliefs for decommissioning, the government has reduced tax rates and made trading assets easier to encourage oil and gas companies to invest in maximising the extraction of the UK's remaining reserves. The government is committed to supporting oil and gas companies due to the industry's role in generating direct tax revenues, supplying energy and providing employment. The Department says that oil and gas will remain an important part of the energy supply: it estimates that oil and gas will provide nearly 70% of total energy required in 2035 and will remain particularly important fuels for transport and domestic heating. But the role of oil and gas in the economy is expected to decline as the government switches support to cleaner renewables to achieve its climate change targets.

Recommendation: ***The Department should set out as part of its energy White Paper, expected during 2019, how it will continue to ensure that government support for oil and gas remains compatible with its wider energy objectives.***

6. **There is uncertainty over whether carbon capture, usage and storage (CCUS) will become a viable option for reusing oil and gas assets.** CCUS could be essential for decarbonising the economy at the lowest cost, but it is currently too expensive to be commercially viable. The Department has stated that the costs of the first CCUS projects could be reduced if oil and gas assets are reused, such as repurposing pipelines to transport carbon dioxide and using wells to store it. This could also defer part of the bill for decommissioning. But, as this Committee has previously reported, the government has tried and failed to support deployment of CCUS twice in the past and there is no imminent prospect of a large-scale CCUS facility being in operation in the UK. There is a risk that oil and gas assets are decommissioned before they can be used for CCUS schemes due to the Department's slow progress at bringing forward CCUS.

   Recommendation: ***The Department should, as part of its Treasury Minute response, set out its expected timetable for CCUS deployment and how this aligns with the latest indications of when oil and gas companies will decommission their assets.***

1 Minimising costs and maximising benefits of decommissioning to the taxpayer

1. On the basis of a report by the Comptroller and Auditor General, we took evidence from the Department for Business, Energy and Industrial Strategy (the Department) and the Oil and Gas Authority (the OGA) on the actions they are taking to reduce the costs to taxpayers of decommissioning offshore oil and gas assets.[1]

2. There are currently around 320 fixed installations, such as oil platforms, in production in the UK, primarily in the North Sea. To date, oil and gas assets have enabled operators to recover more than 44 billion barrels of oil and gas. But reserves are running out, with the remaining oil and gas becoming harder to find and extract. Oil and gas companies in the UK are increasingly decommissioning their assets as they are reaching the end of their useful economic lives and have spent more than £1 billion on decommissioning in each year since 2014. International obligations require the companies operating assets to plug and abandon wells and remove all the surrounding structures, with exceptions in certain circumstances.[2]

3. The OGA estimates that decommissioning will cost companies between £45 billion and £77 billion, with almost all the expenditure coming in the next 20 years. Decommissioning affects the government's finances because oil and gas companies can recover some of their costs through tax reliefs. These enable the companies to deduct decommissioning costs from their taxable profits and potentially claim back some taxes that they have previously paid. HM Revenue & Customs (HMRC) estimates that tax reliefs will cost £24 billion in total.[3] HMRC calculates that it has given tax reliefs for decommissioning worth between £635 million and £965 million in each year since 2013–14 and forecasts that tax reliefs for decommissioning will exceed £1 billion for the first time in 2018–19.[4]

4. The Department has overall responsibility for the safe, cost-effective and environmentally sensitive decommissioning of offshore oil and gas infrastructure. In 2015, the Department established the OGA to regulate the industry, promote the continued extraction of remaining resources and help operators to reduce their decommissioning costs. The Department also monitors the financial health of oil and gas companies and can require companies to set aside money to pay for future decommissioning if it thinks there is a risk of the bill falling to taxpayers.[5]

Uncertainty over the cost to taxpayers

5. The amount that decommissioning will cost oil and gas companies is very uncertain. The OGA produces an annual estimate of the total future cost to oil and gas companies of decommissioning. Its latest estimate, in June 2018, was that decommissioning would cost between £45 billion and £77 billion. The OGA expects 49% of the estimates that feed

1 C&AG's Report, *Oil and gas in the UK – offshore decommissioning*, Session 2017–19, HC 1870, 25 January 2019
2 C&AG's report, paras 1, 2, 2.2, 2.3
3 C&AG's report, paras 9, 11
4 HM Revenue & Customs, *Bulletin: Estimated cost of tax reliefs*, 31 January 2019
5 C&AG's report, paras 4, 14

into this total to be accurate only within a range of -20% to +100% and an additional 40% of estimates to be accurate within -15% to +50%.[6] The OGA told us there is uncertainty over the costs of decommissioning because there are hundreds of installations to be decommissioned over the next 40 years, ranging from projects being decommissioned now to new discoveries where the assets have not even been built yet.[7]

6. HMRC's estimate that future tax reliefs for decommissioning will cost £24 billion is based on the central estimate from the OGA's range, which is £58.3 billion. The actual costs taxpayers will incur is highly uncertain in line with the uncertainty of the OGA's estimate of the decommissioning costs for oil and gas companies, as well as other economic factors that feed into HMRC's estimate, such as future oil prices and exchange rates.[8] The Department was unable to tell us what the cost to taxpayers would be if decommissioning costs were £77 billion, which is the top end of the OGA's range, but it assumes it would be around 40% of that figure.[9] The total bill for decommissioning is also set to grow as the government approves new projects in line with its objective to maximise the recovery of the remaining oil and gas. The OGA told us, for example, it had approved 19 new projects last year, which will be added to future estimates of decommissioning costs.[10]

7. The OGA told us it is taking action to increase the certainty of its decommissioning cost estimate. It explained that it previously highlighted its concerns to the chief executives of the oil and gas companies about the lack of certainty in their estimates, which has resulted in the percentage of estimates being in the least certain category falling from 72% to 49%. The OGA also told us it has plans to state a new expectation of companies that they increase the certainty of the cost estimate three years prior to beginning decommissioning and that it will use its regulatory powers to enforce this if necessary. The Department told us that oil and gas companies are required to estimate their future decommissioning liabilities each year in their audited accounts, which provides an additional incentive for the companies to ensure their estimates are accurate.[11]

Impact of OGA and the Department

8. The OGA has stated that it will work with oil and gas companies to reduce their forecast decommissioning costs by 35% by 2022.[12] It tracks progress towards this target through its annual forecast of future decommissioning costs. In June 2018, it reported that the forecast cost to decommission assets included in both its 2017 and 2018 estimates had fallen by 7%, although new projects offset some of this reduction in the overall estimate.[13] The OGA told us that if oil and gas companies reduce their costs by 35% this would result in a saving to taxpayers of £8.6 billion.[14] The OGA told us that oil and gas companies incurred £1.45 billion of decommissioning expenditure in 2018 but it has not said whether this demonstrates that reductions in estimated decommissioning costs have started to be translated into actual savings.[15]

6 C&AG's report, paras 2.7, 2.8
7 Q 3
8 C&AG's report, para 2.18
9 Q 8
10 Q 9
11 Q 7
12 C&AG's report, para 3.6
13 C&AG's report para 3.16
14 Q 9
15 Q 6

9. The OGA explained that it has helped oil and gas companies to identify savings by showing them how they compare with other companies and sharing best practice. It said, for example, it had shown one company that was expecting to spend £3.6 million to plug and abandon each of its wells that other companies were planning to perform the same activity for just £1 million per well. According to the OGA, this one example resulted in a reduction of £126 million in the estimated decommissioning cost.[16] The Department told us that the success of comparing different companies had caused it to consider how the approach could similarly be used in nuclear decommissioning.[17] The Department also claimed that the OGA's successes had caused other countries around the world to be interested in its work.[18]

10. The Department and the OGA both acknowledged the challenge of isolating the impact of the OGA's work from the wider factors that influence oil and gas companies' decisions. The Department said that, despite the work of the OGA, the costs of decommissioning to taxpayers could increase if oil and gas prices crashed, though it does not expect this to happen, and that the overall economic situation is the biggest factor determining oil and gas companies' decisions.[19] The OGA told us it has done work to address the challenge of measuring its own success when ultimately it is the oil and gas companies themselves that are achieving cost savings. In doing this work it has recorded 22 'successes', which equate to just over £300 million of savings.[20]

Exporting decommissioning skills and resources

11. The UK is the first country to be decommissioning assets in the North Sea. Therefore, the Department sees a lot of potential for exporting decommissioning skills and resources to other countries that are decommissioning later.[21] In the 2018 Budget, the government announced it would work with the OGA to call for evidence to identify ways of strengthening the UK's position as a 'global hub' for decommissioning.[22] The UK and Scottish governments have also established the Oil and Gas Technology Centre (OGTC), which has in turn established the National Decommissioning Centre, in partnership with the University of Aberdeen, as an industry-led centre of excellence set up to deliver research and training in oil and gas decommissioning.[23]

12. We asked the Department what thought it had given to protecting the intellectual property from technology developed using taxpayer money. The Department told us it had not considered this yet but would see to what extent the issue is raised in the responses to its call for evidence.[24] We also asked the Department how it would ensure the government accrues the benefits of developing decommissioning skills and resources rather than companies moving it to other parts of the world. The Department said that, as well as the initial £90 million funding for the OGTC, it has support from the Department for

16 Qq 5, 6
17 Q 37
18 Q 25
19 Qq 14, 25
20 Q 26
21 Q 37
22 C&AG's report para 3.11
23 Q 37; C&AG's report para 3.10
24 Q 42

International Trade and it is planning a seminar with ambassadors from around the UK on the Industrial Strategy where it will market the use of British expertise in oil and gas around the world.[25]

Decommissioning fracking assets

13. Under the Petroleum Act 1998, the government is liable for decommissioning offshore oil and gas assets if oil and gas companies are not able to pay for decommissioning themselves, for example due to insolvency. The risk is partly mitigated because the liability transfers in the first instance to existing partner companies operating the asset, or previous owners of the asset, and only transfers to government if no such companies exist.[26] The Department told us that it focuses on the 20% of offshore assets that have never been owned by one of the largest oil and gas companies and that it can require companies to set money aside for future decommissioning costs if it considers there to be too high a risk of the bill falling to taxpayers. To date, it has asked nine operators to sets aside a total of £844 million and it is negotiating similar arrangements on a further three fields.[27]

14. We asked the Department whether taxpayers could face similar liabilities to decommission onshore fracking assets in the event of the licence holder going out of business. We drew attention to the apparent greater risk than in the offshore industry because fracking is conducted by smaller companies, with less financial backing, meaning they could be short lived. The Department told us that the Secretary of State would consider the ability of a company to meet their decommissioning costs when deciding whether to give consent for operations to commence and can require them to set money aside. The Department said that the Environment Agency, as the regulator for onshore activities, would also consider decommissioning as part of its role.[28] We asked the Department if it plans to produce any additional guidelines to the decommissioning of fracking infrastructure, especially in light of the government's promotion of developing shale gas in the UK. On 12 March, the Department published guidance on fracking,[29] including an assessement of its enivronental and economic impact. It does not, however, provide any information on the decommissioning of fracking infracture.

15. The Department wrote to us after the session to state that the Environment Agency would not allow the surrender of a permit until sites have been returned to a satisfactory condition. According to the Department, if a permit holder company is no longer in existence the Environment Agency would have the ability to pursue former directors from that company and if this was unsuccessful the Environment Agency would identify if there were other appropriate parties who could bear responsibility, such as the landowner.[30]

25 Qq 58–61
26 C&AG's report, para 2.19
27 Qq 11–12
28 Qq 79–95
29 Department for Business, Energy and Industrial Strategy, *Guidance on fracking: developing shale gas in the UK*, 12 March 2019
30 Letter from the Department for Business, Energy and Industrial Strategy, 25 February 2019

2 The government's climate change objectives

Compatibility of support for oil and gas

16. The government wants oil and gas companies to maximise the extraction of the UK's remaining oil and gas reserves because of the industry's role in the economy, supplying energy and supporting jobs. The Oil and Gas Authority (the OGA) estimates that between 10 billion and 20 billion barrels of recoverable oil and gas remain in the UK, in addition to the 44 billion barrels that operators have already extracted. The Department for Business, Energy and Industrial Strategy (the Department) established the OGA in 2015 to support oil and gas companies to maximise the extraction of the remaining resources. Additionally, since 2013 HM Treasury has reduced tax rates and given greater certainty over decommissioning tax reliefs to incentivise continued extraction.[31]

17. The OGA told us that the tax changes had been significant in enabling oil and gas companies to add 3.7 billion barrels of oil and gas to the central production forecast out to 2050, compared to its baseline forecast in 2015. It did not believe that increase would have happened without the tax incentives.[32] It said that further tax changes would be needed for oil and gas companies to extract all the remaining reserves.[33]

18. The government projects that oil and gas will play a smaller role in meeting energy demand over time as reserves run out and it switches its support to cleaner alternatives to achieve its climate change objectives. The Climate Change Act 2008 require the government to reduce carbon dioxide emissions by 80% in 2050 compared with 1990 levels. The Department forecasts that electricity generation from gas will fall by 63% by 2035.[34]

19. We asked the Department whether there is a potential for tension between the government's ongoing support for continued extraction of oil and gas and its obligation to reduce carbon dioxide emissions. The Department told us that it expects with a very high level of confidence that the UK will need a lot more oil and gas for the next 25 years because oil and gas are still heavily depended upon for transport and heating. It said that even as the use of oil and gas in the economy reduced it would expect a higher proportion to come from UK sources rather than imports.[35]

Carbon capture usage and storage

20. The Department regards having carbon capture usage and storage (CCUS) technology operating in the UK to be essential to meet its climate change obligations. This is because of its potential to reduce carbon dioxide emissions across the power and industrial sectors.[36] In November 2018, the Department published its CCUS action plan, which set out how it will be in a position to scale up deployment of the technology in the mid-

31 C&AG's report, paras 1.6–1.13
32 Qq 15–16
33 Q 47
34 C&AG's report, para 1.14
35 Qq 53–54
36 Q 32

2020s.[37] This stated that there is potential for cost savings in initial CCUS projects which can re-use existing oil and gas infrastructure, such as pipelines and wells for transporting and storing carbon dioxide respectively.[38]

21. The Department told us that it is committed to identifying existing infrastructure that might be suitable for re-use and developing a policy on the re-use of infrastructure for CCUS. It said that both of these were to be done in the first half of 2019.[39] The Department also said that it sees CCUS as being a potentially valuable export, which it is looking at as part of its industrial strategy. It said that some of the expertise developed already had been made available to projects in other parts of the world.[40]

22. As the previous Committee reported, the government has previously attempted to support the deployment of CCUS through two separate competitions, which were both unsuccessful in enabling the first CCUS facilities to become operational.[41] The Department told us it had learnt from those competitions the importance of having full commitment of all parties to CCUS to avoid discontinuation of government funding at short notice. The Department's direct support for existing projects is currently relatively small. There is a risk that CCUS deployment will continue to be delayed meaning the timings do not fit with the decommissioning of oil and gas assets.[42]

37 Q 29
38 HM Government, *Clean Growth: The UK Carbon Capture Usage and Storage deployment pathway*, November 2018, page 40
39 Q 27
40 Q 35
41 Committee of Public Accounts, *Carbon Capture and Storage*, 64th Report of Session 2016–17, HC 1036, 28 April 2017
42 Qq 29–35

Formal minutes

Wednesday 20 March 2019

Members present:

Meg Hillier, in the Chair

Sir Geoffrey Clifton-Brown
Caroline Flint
Stephen Morgan
Anne Marie Morris
Bridget Phillipson
Lee Rowley
Gareth Snell

Draft Report (*The public cost of decommissioning oil and gas infrastructure*), proposed by the Chair, brought up and read.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 22 read and agreed to.

Introduction agreed to.

Conclusions and recommendations agreed to.

Summary agreed to.

Resolved, That the Report be the Ninetieth of the Committee to the House.

Ordered, That the Chair make the Report to the House.

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

[Adjourned till Monday 25 March at 3:30pm

Witnesses

The following witnesses gave evidence. Transcripts can be viewed on the inquiry publications page of the Committee's website.

Monday 11 February 2019

Alex Chisholm, Permanent Secretary, the Department for Business, Energy and Industrial Strategy, **Emily Bourne**, Director, Energy Development and Resilience, Department for Business, Energy and Industrial Strategy, and **Andy Samuel**, Chief Executive, The Oil and Gas Authority Q1–99

List of Reports from the Committee during the current Parliaments

All publications from the Committee are available on the publications page of the Committee's website. The reference number of the Government's response to each Report is printed in brackets after the HC printing number.

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