

**EXPLANATORY MEMORANDUM TO THE
EXCISE DUTIES (SURCHARGES OR REBATES) (HYDROCARBON OILS ETC.)
(AMENDMENT) ORDER 2004**

2004 No. 3160

1. 1.1 This explanatory memorandum has been prepared by HM Customs and Excise on behalf of HM Treasury and is laid before the House of Commons by Command of Her Majesty.

1.2 This memorandum contains information for the Select Committee on Statutory Instruments.

2. Description

2.1 This Order amends the Excise Duties (Surcharges or Rebates) (Hydrocarbon Oils etc.) Order 2004 (S.I. 2004/2063) (“the Principal Order”). The Principal Order adjusts the liabilities to excise duty (and rights to rebate in respect of such duty) on the various products cited in the instrument that are chargeable by virtue of the Hydrocarbon Oil Duties Act 1979 (c. 5) (“the Oil Act”). This instrument decreases the percentages specified as additions to the amounts of rebate allowable, such that the amounts payable in respect of the rebated hydrocarbon oils are increased by 1 penny per litre.

3. Matters of special interest to the Select Committee on Statutory Instruments

3.1 The instrument is made under complex powers. This is the first time that the powers have been used to amend an instrument already made under the powers. The interaction of this instrument with the Principal Order, the Oil Act (which has been amended numerous times) and with the changes made to the Oil Act by the Finance Act 2004 (c.12) (the Finance Act”) is complex.

The Excise Duties (Surcharges or Rebates) Act 1979

3.2 This instrument has been made by the Treasury in exercise of their powers under sections 1(2) and 2(3) of the Excise Duties (Surcharges or Rebates) Act 1979 (c. 8) (“the Act”). The Act consolidated the provisions of section 9 of, and Schedules 3 and 4 to, the Finance Act 1961, with the provisions amending them.

3.3 In summary, the Act provides the Treasury with the power, by Order made by statutory instrument, to provide for an adjustment (an increase or decrease) of any liability to certain excise duties (or of any right to drawback, rebate etc. in respect of such duties) by up to 10 per cent. Such an Order ceases to be in force at the expiration of a period of one year from the date on which it takes effect, unless continued in force by a further order.

3.4 The power does **not** extend such as to allow the Treasury to adjust the actual rates of duty or to make textual amendments to the Oil Act (or any other primary legislation) (see section 1(2) to (4) of the Act).

3.5 As first enacted, the Treasury could exercise the power only if “it appears to the Treasury that it is expedient, with a view to regulating the balance between demand and resources in the United Kingdom...”. Further, the adjustment, if made, had to be of every liability to duty within a group or groups of excise duties cited in the Act. However, the Act has been amended by section 10 of the Finance Act 1980 (c. 48), section 10 of the Finance Act 1982 (c. 39) and section 11(4) of the Finance Act 1993 (c. 34) to provide for greater flexibility. In particular, the use of the power is no longer limited by the words quoted above and the Treasury may now provide for the adjustment, by up to 10 per cent, of any liability to duty (or right to rebate) to which the Act applies, and may specify different percentages for different cases.

3.6 A consolidated text of the essential provisions of the Act (insofar as relevant to this instrument) is enclosed with this memorandum at Annex A.

The Oil Act

3.7 Hydrocarbon oil¹ is either “heavy oil” or “light oil”². Section 6(1) of the Oil Act provides that there shall be charged on hydrocarbon oil imported into the United Kingdom, or produced in the United Kingdom, a duty of excise at the rates specified in section 6(1A)³. There are rebates of duty or differential rates of duty for various types of hydrocarbon oil.

3.8 Section 6(1A) of the Oil Act provides for six separate rates of duty on hydrocarbon oil in respect of sulphur-free petrol (“SFP”)⁴, ultra low sulphur petrol (“ULSP”)⁵, light oil other than ULSP and SFP, sulphur-free diesel (“SFD”)⁶, ultra low sulphur diesel (“ULSD”)⁷ and heavy oil other than ULSD and SFD. For convenience, in this memorandum these are termed the “base rates” for hydrocarbon oils. All types of hydrocarbon oil will fall within one of the six categories and, prima facie, will be chargeable at one of the rates specified.

3.9 Rebates of hydrocarbon oil duty are provided for by sections 11⁸, 13AA⁹ and 14¹⁰ of the Oil Act, in relation to what might best be described as non-road fuel use of hydrocarbon oils. Those rebates are expressed in the Oil Act in such a way (“a rebate of duty at a rate of X pence a litre less than the rate at which the duty is chargeable”) that the amounts expressed in sections 11(1) and 14(1) in the Oil Act are the effective

¹ A term defined in section 1(2) of the Oil Act.

² See section 1(3) and (4) of the Oil Act.

³ Section 6(1A) of the Oil Act was last amended by section 4 of the Finance Act 2000 (c.17), section 1 of the Finance Act 2001 (c. 9), section 4 of the Finance Act 2003 (c. 14) and sections 5 and 7 of the Finance Act 2004 (c. 12).

⁴ See section 7 of the Finance Act 2004 (c. 12).

⁵ A term defined in section 1(3A) of the Oil Act, as inserted by section 5 of the Finance Act 2000 (c.17) and substituted by section 7 of the Finance Act 2004 (c. 12).

⁶ See section 7 of the Finance Act 2004 (c. 12).

⁷ A term defined in section 1(6) of the Oil Act, as inserted by section 7 of the Finance Act 1997 (c.16), and substituted by section 8 of the Finance Act 1998 (c. 36) and by section 7 of the Finance Act 2004 (c. 12).

⁸ Relevant amendments were made to section 11 by section 2(2) and (3) of the Finance Act 1986 (c. 41), section 5 of the Finance Act 1996 (c. 8), section 7(5) of, and Part 1 of Schedule 18 to, the Finance Act 1997 (c. 16), section 10(2) of the Finance Act 2000 (c. 17), paragraph 3 of Schedule 2 to the Finance Act 2002 (c. 23), section 5(1) of the Finance Act 2003 (c. 14) and sections 5(3) and 10(5) of the Finance Act 2004 (c. 12)

⁹ Section 13AA was inserted by section 5(4) of the Finance Act 1996 (c. 8) and amended by section 7(6) of the Finance Act 1997 (c. 16) and section 7(6) of the Finance Act 2004 (c. 12).

¹⁰ Relevant amendments were made by section 4(2) of the Finance Act 2003 (c. 14) and section 5(5) of the Finance Act 2004 (c. 12).

rates of duty (that is, the amount payable after the relevant rebate is subtracted from the relevant “base rate” of duty) on those products.

3.10 For example, in the case of the rebate allowed for light oil used as furnace fuel the amount set in section 14(1) of the Oil Act is 6.24 pence per litre. The rebate must be subtracted from the “base rate” for light oil other than ULSP and SFP (which is 57.9 pence per litre). The rebate is (£0.5790 – £0.0624 =) £0.5166. The application of a rebate of £0.5166 to the rate of £0.5790 gives an amount payable of £0.0624.

Effect of the Orders

3.11 In the case of rebated fuels, it is important to note what section 1(4) of the Act says about the adjustment of a rebate under the Act: “in calculating the amount to be adjusted any adjustment under this section of the liability to duty shall be disregarded”. Or, to put it another way, the rebate “bites” on the “base rate” of duty that is set in the Oil Act and the adjusted rebate will also bite on the “base rate” that is set in the Oil Act.

3.12 The purpose of the Principal Order is to negate, temporarily, the effect of the increases in the rates of duty set out in sections 5 and 7 of the Finance Act 2004 (c. 12) (“the Finance Act”), which amends the Oil Act (see below, legislative background at 4.2 to 4.7).

3.13 In the case of the rebated hydrocarbon oils, article 4 of the Principal Order adjusts the amount allowable as rebate by the addition to the amount allowable of the percentage specified in each case. The result is that the amount the person pays (the relevant “base rate” minus the relevant rebate) is reduced. In particular, it is reduced so as to give the same result as if the amendments made by sections 5 and 7 of the Finance Act had not come into force.

3.14 Again, let us take the example of light oil for use as furnace fuel (see section 14(1) of the Oil Act). The object of the Principal Order is to return to the pre-Finance Act position where a person would be liable to pay 3.82 pence per litre (rather than 6.24 pence per litre). To reach the amount payable of £0.0382 per litre, the new rebate must be (£0.5790 – 0.0382 =) £0.5408. That is an increase of (£0.5408 - £0.5166 =) £0.0242, or 4.68% in the amount of the rebate.

3.15 This Order decreases the percentages specified in the Principal Order as additions to the amounts of rebate allowable. For instance, in the case of light oil for use as furnace fuel, the new adjusted rebate allowed is £0.5308. That is an increase from the Finance Act position of (£0.5308 - £0.5166 =) £0.0142, or 2.74% in the amount of the rebate. Thus, the amounts payable (the “base rate” minus the adjusted rebate) in respect of the rebated hydrocarbon oils are increased from the position that obtained under the Principal Order (by one penny per litre). However, the amounts payable (for fuel oil and light oil for use as furnace fuel, £0.0482 per litre, for the other rebated oils, £0.522 pence per litre) are still less than if the Principal Order did not exist. The overall effect of the Principal Order, as amended by this Order, is that persons pay less than if the Orders did not exist. But the effect of this Order compared with the position under the Principal Order alone, is that persons pay more.

3.16 The Committee is respectfully referred to the Order and its explanatory note for the precise rates of rebate that would have obtained but for this Order and the

Principal Order, the rates of rebate that obtain as a result of this Order, and the percentages by which each rate of rebate is adjusted.

Parliamentary Procedure

3.17 This instrument is subject to the “affirmative resolution procedure” by virtue of section 2(7)(b) of the Act.

3.18. Although section 2(7) of the Act does not expressly refer to the adjustments that might be made to rights to rebate etc, it is clearly intended that any Order made under the Act that has the effect of increasing the amount of duty that a person must pay (either by the making of a “surcharging” Order, or the withdrawal or amendment of a “relieving” Order), must be approved by the House of Commons. Any Order that has the opposite effect (either a “relieving” Order, or the withdrawal or reduction of a “surcharging” Order) is subject to annulment in pursuance of a resolution of the House of Commons.

3.19 As explained above, this instrument reduces the percentages specified as additions to the amounts of rebate allowable. Thus, it reduces the deduction from the amount payable in the case of the rebated hydrocarbon oils and increases the amount of duty that a person must pay in respect of those oils.

4. Legislative Background

4.1 The powers conferred by the Act were exercised for the first time by the making of the Principal Order. The similar powers conferred by the Finance Act 1961 (as amended) were exercised on four occasions, most recently in December 1976.

4.2 Section 5 of the Finance Act amended the Oil Act to provide for the rates of excise duty on hydrocarbon oil to be increased by an amount that reflected the rate of inflation (although see what is said below re: the rates for ULSD and ULSP) from 1st September 2004. For those rebated oils listed in Table B of the Principal Order, section 5 of the Finance Act increased the effective rate of duty by the amount required to reduce the differential relative to the main road fuels by 1 penny per litre.

4.3 Section 7 of the Finance Act amended the Oil Act to provide for new rates of duty from 1st September for SFP and SFD. The rates were set at what would have been the revalorised rates for ULSP and ULSD, which SFP and SFD are expected to replace as the most commonly available road fuels. The duty rates for ULSP and ULSD are increased with effect from 1st September in line with inflation plus half a penny per litre.

4.4 In Budget 2004, the Chancellor said that while the oil industry was preparing for the introduction of “sulphur-free” fuels on 1st September 2004, he would “delay for the second year running the annual rise in fuel duty for nearly six months”. Thus, the amendments made by sections 5 and 7 of the Finance Act all came into effect on 1st September 2004.

4.5 After the OPEC meeting in Beirut of 3rd June 2004, the Chancellor of the Exchequer said that the Government planned to review progress in the level of oil prices in August and to decide then whether or not to continue with the duty increase planned for 1st September.

4.6 On 20th July 2004, the Economic Secretary to the Treasury gave the following response to a parliamentary question from Jackie Lawrence MP (Official Report, 20 July 2004, Column 189W):

“On 3 June, in recognition of the pressures in the oil market and because of a shortage of oil supply to meet demand, the Chancellor of the Exchequer announced that we would be reviewing progress of the annual fuel duty increase planned for 1 September.

The Government's focus since 3 June has been on OPEC and oil producers and their responsibilities to meet their own targets on sustainable oil prices, and we have sought to await the outcome of this month's OPEC Ministers meeting before making a further statement. I will give further details of discussions and progress to Members of the House when I appear before the Treasury Select Committee tomorrow.

With the next meeting of OPEC Ministers now moved from July to September, and in light of the continuing uncertainty in the oil market, we have decided to keep the planned increase, including for sulphur-free fuel and rebated fuels, under review, and will report back further at the time of the pre-Budget report. Because of its environmental benefits the Government remain committed to the introduction of sulphur free fuel, and will be in discussion with the industry over its availability across the country. The Chancellor of the Exchequer will also report back on this issue at the time of the pre-Budget report.”

4.7 Therefore, the Principal Order made adjustments to the liabilities to excise duty (and rights to rebate in respect of such duty) with effect from 1st September 2004. The adjustments take effect on the rates that are provided for by sections 5 and 7 of the Finance Act, as soon as those provisions come into force. The practical effect is to reduce all the rates of duty and effective rates of duty amended by sections 5 and 7 of the Finance Act back to the levels that existed before sections 5 and 7 of the Finance Act came into force.

4.8 Following the review by Ministers of the planned duty increases announced in Budget 2004, the Chancellor of the Exchequer reported to the House of Commons on this matter in his pre-Budget report on 2nd December 2004. As a result of that review, the Chancellor confirmed that, in response to the continued volatility in the global oils market, the freeze on the main road fuel duties would be continued for this year.

4.9 The Chancellor also confirmed that he will implement the narrowing of the duty differential by one penny per litre between rebated oils and main road fuels, with the aim of assisting efforts to reduce oils fraud from pre-Budget 2004 levels and in recognition of the fact that that these fuels are more harmful to the environment than other road fuels. This means the effective rate of duty for rebated fuels would be increased partially as originally planned at Budget 2004.

5. Extent

5.1 This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

6.1 The Economic Secretary to the Treasury, John Healey MP, has made the following statement regarding Human Rights:

In my view, the provisions of the Excise Duties (Surcharges or Rebates) (Hydrocarbon Oils etc.) (Amendment) Order 2004 are compatible with the Convention rights.

7. Policy Background

7.1 The rates of fuel duty were increased by the Finance Act as a result of the Chancellor of the Exchequer's Budget 2004. Most of the increases were in line with inflation and were to take effect on 1st September 2004.

7.2 The delayed commencement was to lessen the disruption to oil companies that might otherwise happen from having to make two price adjustments in the course of one year due to duty changes (e.g. once for Budget 2004 and then once again for the introduction of any duty incentive for sulphur-free fuels introduced in September 2004). Furthermore, by delaying introduction of this increase, businesses and motorists would be able to benefit by almost £300 million in terms of duty saved.

7.3 The Government subsequently decided that it wished to keep the changes under review and report back to Parliament at the time of the pre-Budget report.

7.4 Oils fraud is estimated to account for 5% of the UK market for diesel (equivalent to £650 million per year). The large differential between the duty on road fuels and that on rebated oils (the duty rate for ultra-low sulphur diesel, for example is currently 47.10 pence per litre whilst "red" diesel is currently dutied at just 3.82 pence per litre) makes fraud very profitable in this area. The Government's UK Oils Strategy aims to make rebated fuels fraud unattractive as a crime and is focused on stopping large-scale commercial and criminal fraud through a combination of law enforcement activity and better controls on the sale and distribution of the oils involved. The narrowing in the differential between rebated oils and road fuel is only one aspect of a multi-stranded approach, and as such represents a measured and proportionate response.

7.5 In addition, the narrowing of the duty differential for rebated oils is in line with the Government's environmental objectives as set out in their pre-Budget report in 2003. This set out the Government's policy that duty incentives for oils should be commensurate with their environmental benefits. Rebated oils are often less environmentally friendly and more polluting than conventional road fuels. For example, the average sulphur content of red diesel is 1,300 parts per million compared with less than 50 parts per million for ultra-low sulphur diesel.

8. Impact

8.1 A Regulatory Impact Assessment has not been prepared for this instrument as it simply partially implements a duty rate change already included within Finance Act 2004 and which will have no effect on the regulatory impact on business, charities or voluntary bodies.

8.2 There is no regulatory impact on the public sector.

9. Contact

9.1 Michael Lyttle at the Environmental Taxation Development Division, HM Customs and Excise, 1st Floor West, New Kings Beam House, 22 Upper Ground London SE1 9PJ (tel: 020 7865 4770 or e-mail: michael.lyttle@hmce.gsi.gov.uk) can answer any queries regarding the instrument.

Excerpt from the Excise Duties (Surcharges or Rebates) Act 1979, as amended

“1 Surcharges or rebates of amounts due for excise duties

- (1) This section applies to the following groups of excise duties, namely...
 - (b) those chargeable by virtue of the Hydrocarbon Oil Duties Act 1979...
- (2) The Treasury may, by an order applying to one or more of the duties to which this section applies, provide for an adjustment—
 - (a) of any liability to such a duty; and
 - (b) of any right to a ...rebate ...in connection with such a duty,

by the addition to or deduction from the amount payable or allowable of such percentage, not exceeding 10 per cent, as may be specified in the order.

- (3) The adjustment under this section of a liability to duty shall be made where the duty becomes due while the order is in force with respect to it.
- (4) The adjustment under this section of a right to any ... rebate ... in respect of a duty or goods charged with a duty shall be made where the right arises while the order is in force with respect to the duty (whenever the duty became due); but in calculating the amount to be adjusted any adjustment under this section of the liability to the duty shall be disregarded.

...

2 Orders under s 1

- (1) The following provisions of this section shall have effect with respect to orders under section 1 above.
- (2) An order shall cease to be in force at the expiration of a period of one year from the date on which it takes effect unless continued in force by a further order.
- (3) An order—
 - (a) may specify different percentages for different cases; but
 - (b) may not provide for both an addition to any amount payable and a deduction from any other amount payable.

...

- (7) A statutory instrument containing an order which, —
 - (a) specifies a percentage by way of addition to any amount payable or increases a percentage so specified; or
 - (b) withdraws or reduces a percentage specified by way of deduction from any amount payable,shall be laid before the House of Commons after being made; and unless the order is approved by that House before the expiration of twenty-eight days beginning with the date on which it was made, it shall cease to have effect on the expiration of that period, but without prejudice to anything previously done under it or to the making of a new order.

...

- (8) A statutory instrument containing an order to which subsection (7) above does not apply shall be subject to annulment in pursuance of a resolution of the House of Commons.”