EXPLANATORY MEMORANDUM TO

THE HYDOCARBON OIL AND BIOBLEND (PRIVATE PLEASURE –FLYING AND PRIVATE PLEASURE CRAFT) (PAYMENT OF REBATE ETC.) REGULATIONS 2008

2008 No. 2599

1. This explanatory memorandum has been prepared by HM Revenue and Customs and is laid before Parliament by Command of Her Majesty.

2. Description

This instrument, which comes into force on 1st November 2008, provides for the arrangements under which heavy oil (including kerosene) or bioblend on which a rebate of excise duty has been allowed under the Hydrocarbon Oil Duties Act 1979 (c.5) ("the Act") may be used for private pleasure- flying or as fuel for propelling a private pleasure craft on payment of an amount equivalent to the rebate.

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

None

4. Legislative Background

4.1 Sections 13AC and 14E of the Act are inserted by the Finance Act 2008 (c.9) with effect from 1st November 2008[1]. Section 24(1) of the Act is also amended with effect from the same date to enable the Commissioners to make Regulations for any of the purposes of those sections[2].

4.2 Accordingly, this is the first exercise of the powers contained in sections 13AC(3) and (6), 14E(3) and (7) and section 24(1), as amended.

4.3 Section 13AC prohibits the use of kerosene on which a rebate of excise duty has been allowed as fuel for private pleasure-flying unless the person to whom it is supplied makes a declaration in the way and form specified by or under regulations that the kerosene is to be used for such purposes and pays, in accordance with regulations, an amount equivalent to the rebate that has been allowed.

4.4 Section 14E prohibits the use of heavy oil or bioblend on which a rebate of excise duty has been allowed unless the person to whom it is supplied makes a declaration in the way and form specified by or under regulations. If such a declaration is made the supplier must pay, in accordance with regulations, an amount equivalent to the rebate that has been allowed.

4.5 It is therefore necessary to exercise the powers in sections 13AC(6), 14E(7) and the amended section 24(1) before sections 13AC and 14E of the Act come into force for the purposes of giving full effect to those provisions at the time they come into force[3].

4.6 The amendments to the Act and this instrument are being made so as, in effect, to charge excise duty on fuel used for private pleasure-flying and for propelling private pleasure craft, which the UK is obliged to do under Council Directive 2003/96/EC[4] on restructuring the Community

[1] See Schedule 6, paragraphs 11, 15 and 37.
[2] See the Finance Act 2008 (c.9), Schedule 6, paragraph 16. Section 24(1) was also amended with effect from 1st April 2008 by the Finance Act 2008, Schedule 5, paragraph 20.
[3] in reliance on section 13 of the Interpretation Act 1978.
[4] OJ: L283, 31.10.2003, p.51.

framework for the taxation of energy products and electricity (commonly referred to as the Energy Products Directive), following the expiry of derogations from that Directive that the UK enjoyed relating to air navigation and navigation in private pleasure craft (see section 7).

5. Extent

This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

7. Policy Background

7.1 Council Directive 2003/96/EC (the Energy Tax Directive, but usually referred to as the Energy Products Directive (EPD)) sets out which energy products should be liable to tax, the uses that make these products liable to tax and the minimum rates of taxation applicable to each product depending on whether it is used as a propellant, for industrial and commercial purposes or for heating. It also sets out specific exemptions from the normal rules of taxation.

7.2 The Directive sets out in its annexes a number of derogations which allow Member States to apply reduced rates or exemptions from energy tax for various products and purposes. The UK held three derogations to the EPD on

- Fuel used in navigation in private pleasure craft which allowed the use of partially rebated gas oil (red diesel);
- Fuel used for private pleasure-flying which allowed the UK to exempt aviation turbine fuel (avtur) from excise duty (and also to apply a reduced rate on aviation gasoline (avgas) which is not the subject of this instrument)); and
- Waste oils reused as fuel.

7.3 In October 2006 the UK submitted a request for the derogations to be renewed. However, the European Commission did not approve that request and the derogations expired on the 31st December 2006. The Government made a commitment to introduce the changes needed to implement the requirements of the EPD with effect from 1st November 2008.

7.4 Consultation exercises were held from 1st August to 31st October 2007 and followed informal discussions with stakeholders in both sectors. The consultation documents set out a number of options, including the Government's preferred options.

7.5 Five hundred and fifteen responses were received to the consultation on fuel used in private pleasure craft. Most responses were received from private individuals but a number of organisations which responded represented very large numbers, and across a broad spectrum of interests in the marine and inland waterways industry, both commercial and private, including both suppliers and users. The overwhelming response was for the continued use of diesel on which a rebate has been allowed (commonly referred to as "red diesel"), mainly for reasons of supply; typically suppliers of red diesel supply to both commercial and private users and the supply infrastructure already exists.

7.6 Twenty five responses were received to the consultation on fuel used for private pleasure flying from private individuals, representative bodies and a fuel producer. The Government proposal for a self regulatory scheme for the use of aviation turbine fuel ("avtur") (which is a form of kerosene) for private pleasure flying was accepted.

7.7 The requirement to pay an amount equivalent to the rebate allowed on red diesel or rebated bioblend used for propelling private pleasure craft will raise in the region of £10 million for the exchequer. Private pleasure use of avtur, and therefore the revenue impact, is considered negligible.

7.8 During and after the consultation period HMRC officials also held meetings with representative organisations of those most likely to be affected by the changes.

7.9 Waste oils reused as fuel is the subject of another instrument Hydrocarbon Oil (Supply of Rebated Heavy Oil) (Payment of Rebate) Regulations 2008 (S.I. 2008 No. 2600).

8. Impact

8.1 Full and final Impact Assessments prepared for the amendments made to the Finance Act 2008 are attached to this memorandum. It is confirmed that the figures are still up to date.

8.2 The impact on the public sector is likely to be insignificant.

9. Contact

Dave Fitzgerald at HM Revenue and Customs Tel: 0207 147 0251 or e-mail: dave.fitzgerald1@hmrc.gsi.gov.uk can answer any queries regarding the instrument.

Summary: Intervention & Options

Department /Agency: HM Revenue and Customs	**Title:** Impact Assessment of the implementation of the Energy Products Directive on private pleasure flying	
Stage: Final Proposal	**Version:** 1	**Date:** 14 February 2008

Related Publications: Impact Assessment of the implementation of the Energy Products Directive on private pleasure boats.

Available to view or download at:

http://www.hmrc.gov.uk

Contact for enquiries: Catherine Mawer **Telephone:** 0207 147 0655

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

The derogation from the European Energy Products Directive (EPD) which allowed the UK to charge a reduced rate of duty on aviation gasoline (Avgas) and to exempt aviation turbine fuel (Avtur) used in private pleasure-flying expired on the 31 December 2006. The UK is in breach of European legislation and as such is liable to infraction proceedings by the European Commission. The Government announced at Budget 2007 that the changes needed to implement the requirements of the EPD would be introduced with effect from 1 November 2008.

What are the policy objectives and the intended effects?

To implement the terms of the EPD by making fuel used for private pleasure-flying liable to excise duty while ensuring that the impact of new regimes and procedures have the minimum impact on business.

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

Following a formal consultation on options for change which was held 1 August - 31 October 2007, the final proposals are:

Avtur: Purchaser/user liable for duty payment. Supplier obliged to draw attention to end-use liabilty and if the purchaser intends to use fuel for private pleasure-flying he will be asked to make a written declaration to that effect which the supplier will retain.

Avgas: New free-standing rate of duty on Avgas for both commercial and pleasure use; procedure mirrors the current situation.

When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects? Compliance cost will be reviewed after 3 years.

Ministerial Sign-off For final proposal/implementation stage Impact Assessments:

I have read the Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) the benefits justify the costs.

Signed by the responsible Minister:

Angela Eagle

....Date: 20th February 2008

Summary: Analysis & Evidence

Policy Option: a)	Description: the imposition of kerosene duty on the use of Avtur for private pleasure-fyling

COSTS	**ANNUAL COSTS**		Description and scale of **key monetised costs** by 'main affected groups'	
	One-off (Transition)	**Yrs**	HMRC - One-off set up costs and/or system changes HMRC - Approx £30,000 to £35,000 ongoing costs each year Individual tax payers - Approx £10,000 to £30,000 compliance costs each year	
	£ Negligible			
	Average Annual Cost (excluding one-off)			
	£ 40,000 to 65,000		**Total Cost** (PV)	**£ Ongoing**
	Other **key non-monetised costs** by 'main affected groups' Small costs for suppliers, purchasers and users of Avtur in terms of awareness of the changes. Possible small effect on competition between fuel suppliers from a reduction in demand for Avtur for private pleasure flying but not expected to be significant. HMRC's extra enforcement costs have not been estimated.			
BENEFITS	**ANNUAL BENEFITS**		Description and scale of **key monetised benefits** by 'main affected groups'	
	One-off	**Yrs**		
	£			
	Average Annual Benefit (excluding one-off)			
	£ Negligible		**Total Benefit** (PV)	**£**
	Other **key non-monetised benefits** by 'main affected groups' Avoids infraction proceedings by the European Commission. There will be a small impact on carbon emissions from a reduction in demand for Avtur for private pleasure flying and a new duty rate for Avgas but this is not expected to be significant or quantifiable.			

Key Assumptions/Sensitivities/Risks Estimates of compliance costs are highly dependant on the number of aircraft and the time taken to keep records and submit duty returns and payments for individual aircraft owners. Central estimate of roughly 500 tax payers. Exchequer impact is expected to be negligible.

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

What is the geographic coverage of the policy/option?			UK	
On what date will the policy be implemented?			1 November 2008	
Which organisation(s) will enforce the policy?			HMRC	
What is the total annual cost of enforcement for these organisations?			£ Negligible	
Does enforcement comply with Hampton principles?			Yes/No	
Will implementation go beyond minimum EU requirements?			Yes	
What is the value of the proposed offsetting measure per year?			£	
What is the value of changes in greenhouse gas emissions?			£ Negligible	
Will the proposal have a significant impact on competition?			No	
Annual cost (£-£) per organisation (excluding one-off)	Micro **~ £20-40**	Small **~ £20-40**	Medium **~ £20-40**	Large **~ £20-40**
Are any of these organisations exempt?	No	No	N/A	N/A

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

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

Background

1. Until 31 December 2006, the UK held a derogation from the European Energy Products Directive (2003/96) which allowed the UK to charge a reduced rate of duty on Avgas and to exempt Avtur used for private pleasure flying. The UK derogations had in fact been time-limited since the predecessor to the EPD was agreed and signed in 1992. In 2001, the Government negotiated an extension to the derogation to 31 December 2006. Although the UK submitted a request in October 2006 for the derogation to be renewed again the European Commission did not accept the UK's arguments and the derogation expired on the 31 December 2006.

2. At the Budget 2007 the Government made a commitment to introduce the changes needed to implement the requirements of the EPD with effect from 1 November 2008. The Government also made a commitment to consult formally on the new regimes.

3. Two fuels are used in aviation, Avtur and Avgas. Avtur is mainly used in commercial jet and turbo-prop aircraft, and private pleasure use is considered to be negligible. In its review of the derogations in June 2006 (COM(2006)342), the Commission itself acknowledged this by stating that small light aircraft used in pleasure-flying used a different fuel from jets or commercial aircrafts. Avgas is used in smaller piston-engined aircraft, which are used for both commercial and business purposes as well as for pleasure-flying.

4. There are no official statistics concerning the consumption of either Avgas or Avtur for private pleasure-flying and so it is extremely difficult to accurately assess the private use of either fuel. There is no reason or obligation for the industry to keep any such records, but estimates are that private pleasure use of Avtur is a fraction of one per cent of total use (total Avtur sales in 2005 – the latest year for which we have figures – were 17.5 billion litres), whereas private pleasure use of Avgas is estimated at about 20 per cent of total use (total Avgas sales in 2006 were 31 million litres). The General Aviation sector is the main consumer of Avgas, although General Aviation activities also use Avtur. The General Aviation sector is diverse, covering all flying other than that performed by the major airlines and Armed Services, and includes business aviation, air taxis, flying in support of the emergency services, air ambulances, training for professional and private pilots, aerial photography and surveying.

5. The options which were the subject of the consultation exercise were developed taking into account the views of a number of representatives from the aviation sector, including The British Business and General Aviation Association, the Aircraft Owners' and Pilots' Association, the Popular Flying Association and the British Helicopter Advisory Board. Other Government Departments, including the Department for Transport, were also consulted. The following final proposals are now made having taken into account the results of that consultation exercise.

Avtur

Purchaser/user liable for the payment of the duty

6. All Avtur is currently exempt from duty by virtue of being fully rebated under the Hydrocarbon Oil Duties Act 1979 (HODA) section 11(1)(c). Avtur will remain fully rebated but private pleasure use of Avtur will no longer benefit from the rebate and will be liable to the full rate of duty for kerosene, currently 56.94 pence per litre.

7. The responsibility for paying the duty due will lie with the purchaser and/or the user of the fuel who will be required to make a declaration and pay duty to HMRC if the fuel is used for private pleasure-flying purposes.

Compliance costs for individuals/businesses

8. The following obligations will be placed on individuals who use Avtur for private pleasure-flying who will be required to make a tax return to HMRC and pay duty:

- An obligation to keep records of fuel purchased; and
- An obligation to submit a tax return.

The following ongoing compliance costs have been estimated (central estimate):

Rate of compliance assumed	100%
Returns each year	1
Hours per return *	2
Cost per hour spent **	£20
Total individuals affected ***	500
Total cost each year	**£20,000**

* One hour each year for record keeping and one hour each year for submitting the return
** Hourly wage rate based on HMRC's admin burdens database
*** Estimate based on a 2006 civil aviation authority survey of general aviation

9. However, since the estimate is uncertain it is more appropriate to present a range of compliance costs of between £10,000 and £30,000 which could result from varying assumptions such as the length of time spent completing annual returns, the numbers affected or the average wage rate.

10. Registered Dealers in Controlled Oils (RDCOs) have a duty of care when selling or delivering Avtur to ensure that they only make supplies to customers who have a legitimate use for the oil. This will be extended so that if the RDCO thinks that the fuel might be used for pleasure-flying, he will, under his general duty of care, draw attention to the purchaser of his obligation to contact HMRC and pay the duty due. The RDCO will be required to note his records accordingly. If the purchaser intends to use the fuel for private pleasure-flying, the RDCO will ask him to make a declaration to that effect which the RDCO will retain.

11. There will be a small increased compliance burden on RDCOs familiarising themselves with the changes, informing the purchaser of the duty liability and noting records if they think they might be supplying Avtur for private pleasure-flying and retaining the written declarations.

<u>HMRC costs</u>

12. There will be:

- one-off administration costs for HMRC, including set up costs and/or system changes;
- ongoing costs for HMRC in processing tax returns, estimated at roughly £30,000 to £35,000 a year;
- assurance costs for HMRC in following up sales of possible private-pleasure use fuel as noted in RDCOs' records to ensure that duty has been paid; and
- some legislative changes will be required regarding the RDCOs' obligations and concerning the payment scheme for the purchaser/user.

<u>Competition assessment</u>

13. An increase in the price of Avtur through taxation is likely to reduce the demand from owners/users of private pleasure aircraft. There may be a small knock-on effect on suppliers but this is unlikely to be significant since Avtur is a widely available fuel and this should not directly limit the number or range of suppliers (the vast majority of Avtur is used by commercial aircraft).

14. It is also unlikely that consumers will switch to Avgas due to the cost of converting aircraft engines. More generally, there are unlikely to be adverse competition effects on the sector in terms of reducing the ability of or incentives for suppliers to compete vigorously.

Exchequer and carbon impacts

15. The revenue and carbon impacts of the change are likely to be negligible since the use of Avtur for private pleasure flying is considered to be very small – estimated at a fraction of one per cent of total Avtur use.

Avgas

New separate duty rate for Avgas

16. Avgas is currently liable to a reduced rate of duty whether or not it is used for commercial or private use. The duty rate is set at half of the leaded petrol rate (HODA section 6(3)).

17. Under Article 5 of the EPD, a different duty rate may be introduced for fuel on the basis of product quality as long as it is above the minimum rates laid down in the Directive.

18. Avgas is a significantly different product to leaded petrol. The civil aviation authority only permits the use of road fuel in aviation engines in specific circumstances and prohibits its use in many aircraft engines for safety reasons, hence the higher specification of Avgas. It is tightly controlled during production, and requires specific transport and storage arrangements by oil companies and aerodrome managers for safety reasons. The reasons for which Avgas can be considered to be a different product from leaded petrol include that it has a more complex and more expensive distillation process than for other fuels with specific requirements to meet the special safety demands of aviation; which means that it cannot legally be used as road fuel.

19. A new fiscal definition for Avgas with a new duty rate, respecting the minimum rates permitted under the Directive, will be introduced in HODA. The new rate will apply to all Avgas irrespective of whether it is used for commercial, business or private purposes, in the same way that the current reduced rate is applied.

20. There are a number of advantages to this solution:

- No change to current procedures – no burdens on industry and no effect on supply chains;
- No additional administrative costs for HMRC;
- Minor legislative changes only required; and
- No need to distinguish between commercial and private pleasure use, all Avgas charged at the new rate.

Specific Impact Tests

21. There are no compliance cost impacts from this option on individuals or businesses since it represents the status quo. There may be small revenue and/or carbon impacts to the extent that the new duty rate for Avgas differs from the existing rate.

Specific Impact Tests: Checklist

Use the table below to demonstrate how broadly you have considered the potential impacts of your policy options.

Ensure that the results of any tests that impact on the cost-benefit analysis are contained within the main evidence base; other results may be annexed.

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

Summary: Intervention & Options

Department /Agency:	**Title:**	
HMRC	**Impact Assessment of the implementation of the Energy Products Directive (EPD) on private pleasure boats**	
Stage: Final Proposal	**Version:** [1]	**Date: 14 February 2008**

Related Publications: Impact Assessment of the implementation of the Energy Products Directive on private pleasure flying

Available to view or download at:

http://www.hmrc.gov.uk

Contact for enquiries: Dave Fitzgerald **Telephone:** 0207 147 0251

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

Private pleasure boats were permitted, under an EU derogation, to use marked rebated fuel (red diesel) for propulsion purposes. This derogation expired in December 2006 despite the UK submitting an application for renewal. The use of red diesel for domestic purposes (to generate heat and light), however, is still permitted, as is its use by commercial vessels for propulsion.

The Government needs to implement a scheme that ensures that we comply with the terms of the Energy Products Directive (EPD), while taking all of these factors into account.

What are the policy objectives and the intended effects?

To implement a scheme to comply with the EPD which:

a) minimises the tax and administrative burdens on the industry;

b) recognises that rebated fuel can still legitimately be used for domestic purposes; and

c) is proportionate to the revenue at risk.

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

Following formal consultation on options for change which was held 1 August -31 October 2007, the final proposal is:

private pleasure vessels will continue to be permitted to use marked fuel (red diesel) but at the rate for heavy oil, repaying the rebated duty via the Registered Dealers in Controled Oils (RDCOs) who will declare this to HMRC. An allowance for domestic use will be permitted.

When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects? Compliance cost will be reviewed after 3 years.

Ministerial Sign-off For final proposal/implementation stage Impact Assessments:

I have read the Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) the benefits justify the costs.

Signed by the responsible Minister:

Angela Eagle.. 20th February 2008

Summary: Analysis & Evidence

Policy Option:	Description:

COSTS

ANNUAL COSTS		Description and scale of **key monetised costs** by 'main affected groups'
One-off (Transition)	**Yrs**	Registered Dealers in Controlled Oils (RDCOs) - One-off familiarisation costs and setting up systems and ongoing costs processing fuel transactions and making duty returns & payments HMRC - Small systems changes and processing costs
£ Negligible		
Average Annual Cost (excluding one-off)		
£ 1-1.5 million		**Total Cost** (PV) **£ Ongoing**

Other **key non-monetised costs** by 'main affected groups' Small (mainly one-off) costs for boat owners and users in terms of general awareness of the changes and in providing evidence to RDCOs of commercial use. HMRC's extra enforcement costs have not been estimated. Possible small effect on competition between fuel suppliers but not expected to be significant.

BENEFITS

ANNUAL BENEFITS		Description and scale of **key monetised benefits** by 'main affected groups'
One-off	**Yrs**	Reduction in carbon dioxide emissions from lower use of gas oil (red diesel) for private pleasure boating
£		
Average Annual Benefit (excluding one-off)		
£ 0.15-0.4 million		**Total Benefit** (PV) **£ Ongoing**

Other **key non-monetised benefits** by 'main affected groups' Avoids infraction proceedings by the European Commission. Other environmental and air quality benefits from a reduction in pollutants such as nitrous oxides and sulphur dioxide.

Key Assumptions/Sensitivities/Risks Estimates of compliance costs are highly dependant on the time taken for RDCOs to process fuel transactions, keep records and submit duty returns and payments. HMRC estimate up to 500 RDCOs could be affected. Exchequer impact estimated at roughly + £10 to 15 million in a full year depending on the domestic allowance.

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

What is the geographic coverage of the policy/option?			UK	
On what date will the policy be implemented?				
Which organisation(s) will enforce the policy?			HMRC	
What is the total annual cost of enforcement for these organisations?			£ Negligible	
Does enforcement comply with Hampton principles?			Yes/No	
Will implementation go beyond minimum EU requirements?			Yes/No	
What is the value of the proposed offsetting measure per year?			£	
What is the value of changes in greenhouse gas emissions?			£ 0.15-0.4 million	
Will the proposal have a significant impact on competition?			No	
Annual cost (£-£) per organisation (excluding one-off)	Micro ~ £2-3k	Small ~ £2-3k	Medium ~ £2-3k	Large ~ £2-3k
Are any of these organisations exempt?	No	No	N/A	N/A

Impact on Admin Burdens Baseline (2005 Prices) (Increase - Decrease)

Increase of £ 1-1.5m Decrease of £ 0 **Net Impact** £ 1-1.5 million

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

[Use this space (with a recommended maximum of 30 pages) to set out the evidence, analysis and detailed narrative from which you have generated your policy options or proposal. Ensure that the information is organised in such a way as to explain clearly the summary information on the preceding pages of this form.]

Background

1. UK legislation on oils taxation is contained in the Hydrocarbon Oil Duties Act 1979 (HODA). The EU legislation governing mineral oils structure and rates was contained in three directives (92/80/EEC, 92/81/EEC and 92/82/EEC) which sought to harmonise the treatment of mineral oils for taxation purposes. Some aspects of HODA were incompatible with the directives; however, derogations were negotiated to cover these inconsistencies. These expired on 31 December 2006.

2. The mineral oils directives were repealed by the introduction of the EPD in 2004. This removed the need for some of the derogations; however; the remaining ones retained their expiry date of 31 December 2006. One of these derogations related to the treatment of fuel used in private pleasure boats. Under the terms of the mineral oils directives and then subsequently the EPD, fuel for private pleasure boats was to attract the full rate of duty. The derogation permitted the UK to charge duty for this fuel at the rebated rate.

3. The UK applied for renewal of the derogation; however, our application was rejected on the grounds that, since the fuel had been taxable in principle since 1993, Member States had had enough time to adapt to the requirements of community law. The Commission also did not accept our case that there would be additional administrative burdens or compliance costs resulting from the expiry of the derogations. They stated that if such arguments were to be accepted then the derogation would need to be maintained indefinitely, contradicting the principles that derogations are time limited and introduced with the aim of assisting with initial difficulties encountered with the introduction of new regimes.

4. Ministers announced in Budget 2007 to implement changes to meet the requirements of the EPD with effect from November 2008, with legislation in Finance Bill 2008. The Government also made a commitment to consult on the new regimes.

5. Prior to consulting, we met informally a number of stakeholders who expressed concern at the expiry of the pleasure boat derogations, seeking information and their views in order to develop a number of options. These organisations were:

- The Royal Yachting Association (RYA)
- The British Marine Federation (BMF)
- The Inland Waterways Association (IWA)
- The Federation of Petroleum Suppliers (FPS)
- The Residential Boat Owners' Association (RBOA)

6. Commercial craft are unaffected by the expiry of the derogation and can continue to use rebated fuel.

7. Ministers said that we would look for ways of implementing the new regime which would both minimise the impact, and ensure that any additional compliance burden was as small as possible.

Consultation

8. The formal consultation exercise was held from 1 August – 31 October 2007. Three options were put out to consultation:

1. continued use of red diesel for private pleasure boating but at the full rate of duty with the supplier collecting the duty on the sales. This would extend the current obligations of Registered Dealers in Controlled Oils (RDCOs);
2. continued use of red diesel for private pleasure boating but at the full rate of duty with the user paying the duty direct to HMRC; and
3. switch to unmarked fully paid Ultra Low Sulphur Diesel (ULSD) for private pleasure boating.

Views were also sought on the possibility of a certification scheme for house boats which use red diesel for domestic but not propulsion purposes.

9. These options were drawn up taking into account the current position :

- Private pleasure craft are currently able to use red diesel on which duty has been partially rebated;
- The supply infrastructure supports use of red diesel as most suppliers of fuel to the boat industry provide only rebated red diesel; fuel sites are typically located in harbours, marinas, on floating barges and on towpaths. Supplying a second fuel stream would involve substantial cost for suppliers (new pumps and tanks are estimated at £20,000);
- That of the approximate 500,000 private pleasure boats in the UK, 350,000 are motor boats and depend upon engines for propulsion. Some of these will be residential in nature and also use their engines to provide energy for heat and light.
- Private pleasure boats are currently able to use rebated fuel legitimately both for propulsion and to provide heat and light. The cost of fitting a second tank, where space is available would vary depending on the size and type of boat; estimated at around £750 for a typical inland cruiser.

Final proposed scheme

10. The consultation exercise provided support for the continued use of red diesel with the supplier liable for the charging and accounting for duty. A significant number of responses proposed that fuel used for heating and lighting should not be taxed at the full duty rate since there is no requirement to do so under the EPD.

11. Following the results of the formal consultation exercise the final proposal is that:

- Private pleasure vessels will continue to use marked fuel (red diesel) but at the rate for heavy oil, repaying the rebated duty via the RDCOs who will declare this to HMRC. The rebated rate of duty is currently 9.69 ppl; the full rate is currently 56.94 ppl.
- An allowance for domestic use will be permitted.

12. The benefit of continuing to use marked fuel is that the supply infrastructure is already in place, and existing equipment and tankage can continue to be used. Fuel will continue to be available to pleasure craft throughout the UK, and there will be no restraint on pleasure cruising as a result of pleasure craft being unable to refuel.

Compliance costs for boat owners/users and business

13. This solution will impose a number of burdens on fuel suppliers and boat owners. Rebated fuel is supplied only by Registered Dealers in Controlled Oils (RDCOs) who are required to maintain records of their sales. RDCOs who supply fuel to private pleasure craft will be required to identify such sales, charge the higher rate of duty at the point of sale and pay this to HMRC when they submit their return. To take into account RDCOs' concerns at their ability to distinguish commercial users from private pleasure users, if the supplier is unsure of the use to which the fuel is to be put, the purchaser of the fuel will be required to self certify that status of the vessel as commercial or private and to produce evidence of commercial status and entitlement to the rebated rate. If no evidence is provided to the supplier the purchase will be charged the full duty rate. *Guidance on this issue will be developed.*

14. The existing RDCO scheme does not require RDCOs to make payments of duty. RDCOs are required to simply record and declare to whom they have made sales of rebated fuel. The level of detail RDCOs are required to declare on their returns varies depending on the volume and nature of the sale. For example for domestic sales under 3500 litres and retail or pump sales only the total volume sold and the total number of sales is required. For higher volume sales individual transaction details are required. This reflects the fact that the RDCO scheme was introduced to track the sale of large quantities of rebated fuel.

15. Requiring RDCOs who supply fuel to private pleasure craft to collect and account for duty on retail or pump sales will increase the administration burden on them. It will also place a compliance obligation on them as they will need to charge marked fuel at the higher rate unless the purchaser provides evidence of entitlement to the rebated rate. In order for them to satisfy HMRC that the correct rate has been charged they will need to keep records of their individual retail sales.

16. We will hold further discussions with key stakeholder groups to agree a scheme whereby boat users will also be asked to certify the proportion of fuel which they intend to use other than for propulsion. The scheme will build on the self certificate system proposed above to enable RDCOs to distinguish commercial from private use, and the allowance will be made at the time the fuel is purchased.

<u>RDCOs</u>

17. This scheme will impose the following obligations on RDCOs:

- An obligation to keep records of taxpayers paying the higher rate of duty on rebated oil; and
- An obligation to collect and account for the duty to HMRC.

One-off compliance costs for RDCOs will mainly involve some time spent familiarising themselves with the changes and ensuring suitable record keeping and payment systems are in operation. These costs are not expected to exceed an average of £200 per business, for the estimated 500 RDCOs who will be affected.

18. Based on RDCOs submitting an annual return, which HMRC estimates could take approximately 4 hours to complete, and using average wage rates for businesses submitting HO10 (oils duty) returns from HMRC's admin burdens database, an estimate for these ongoing compliance costs is approximately £50,000 a year.

19. In addition, fuel suppliers will need to process individual fuel transactions and charge duty to private pleasure boat users, including making a suitable adjustment for a domestic allowance. This is expected to take no more than an extra 5 minutes per transaction (and is likely to be less once the changes bed in). Based on an estimated 750,000 private pleasure boating transactions a year, and a wage rate of £20 per hour, these ongoing compliance costs are estimated at around £1.25 million each year.

20. The estimates above are uncertain and it is therefore appropriate to present a range for overall ongoing compliance costs of between £1 million and £1.5 million which could result from varying assumptions such as the length of time spent processing fuel transactions and completing annual duty returns, the numbers affected (both RDCOs and fuel transactions) and average wage rates.

Commercial boat owners

21. Commercial boat owners will need to provide evidence of commercial use if requested by the fuel supplier to continue to use rebated gas oil. This might take the form of an operators' licence or health and safety certificate, for example. In many cases this will only need to be done once at the outset because the fuel supplier will make a note in their records for future reference, and therefore such costs are expected to be minimal.

HMRC costs

22. The changes will also impose some administrative costs on HMRC who will need to devise and operate a compliance and enforcement regime and process duty returns and payments. However, the intention is to use existing HMRC systems and processes to do this work and so any extra costs will be low in relation to the additional revenues collected.

Exchequer impact

23. HMRC estimates that the revenue gain from the expiry of the boat derogation will be broadly in the range £10 to £15 million in a full year taking account of an allowance for domestic use, although the precise details and workings of such an allowance are still to be decided following discussions with those affected. Taken in the context of total hydrocarbon oils duty revenues of £25 billion a year, the private pleasure boat sector will account for a fraction of one per cent of total revenues.

Carbon and environmental impact

24. The loss of the derogation increases the price of fuel for private pleasure boat propulsion which, other things equal, will reduce the amount of fuel used for this purpose. This has a direct carbon and environmental benefit. It is estimated that private pleasure craft have the following carbon impact:

Year	2007
Fuel used for private pleasure boating *	37 million litres
Converted to tonnes **	32,000 tonnes
Amount of carbon per tonne of fuel ***	0.85 tonnes
Total amount of carbon	27,000 tonnes
Social cost of carbon per tonne ***	£95
Total carbon cost of private pleasure boating	£2.6 million

* HMRC estimate based on RDCO returns (including domestic use)

** Using a conversion factor of 1,161 litres of gas oil per tonne

*** Source: Department for Environment Food and Rural Affairs

25. The carbon benefit from the loss of the derogation depends on the extent of the reduction in fuel use following an increase in price through taxation. In line with most fuels, the demand for private pleasure boating use is expected to be relatively insensitive to price changes (‘inelastic’), although it is expected that prices for gas oil could more than double after the duty change and the following table estimates a range of possible carbon benefits arising from a reduction in fuel use.

	Lower estimate	Central estimate	Upper estimate
Reduction in fuel use for propulsion (illustrative)	10%	20%	30%
Carbon benefit	£0.15 million	£0.25 million	£0.4 million

26. There will also be other environmental benefits from a reduction in fuel use for private pleasure boating – mainly improvements in air quality from reductions in pollutants such as sulphur dioxide but these have not been quantified in this assessment.

Competition assessment

27. The loss of the derogation will increase the price of fuel for private pleasure boat use. Other things equal, this will reduce the volume of sales which could have a knock-on impact on the profit margins of some suppliers, at least initially, which in turn could lead to a reduction in the number of suppliers. However, the overall competition effect is expected to be small because gas oil is a widely available fuel and the changes are not expected to significantly raise the costs of new fuel suppliers relative to existing fuel suppliers or limit the ability of, or the incentive for, fuel suppliers to compete vigorously.

Specific Impact Tests: Checklist

Use the table below to demonstrate how broadly you have considered the potential impacts of your policy options.

Ensure that the results of any tests that impact on the cost-benefit analysis are contained within the main evidence base; other results may be annexed.

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