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Legal Update
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Shale gas: the UK announces tax incentives

On 8 October 2012, the Chancellor of the Exchequer, George Osborne, announced that the British Government will soon be consulting on *"a generous new tax regime for shale so that Britain is not left behind as gas prices tumble on the other side of the Atlantic"*.

Background

Readily accessible oil and gas reserves are declining and consequently gas imports are rising rapidly. The energy supply industry is increasingly turning to unconventional reserves to fill the gap left by the decline of coal energy and the unreliability of renewable energy.

Interest in exploiting shale gas reserves has increased with the recent growth of shale gas production in the US and high natural gas prices in the UK. In the US, shale gas now accounts for 23% of domestic gas production and 22% of domestic consumption, helping to reduce natural gas prices in the US to a quarter of UK prices. Whilst the prospects of reductions of this magnitude are unlikely in the UK, the Government clearly sees the exploitation of shale gas as potentially having significant benefits for British consumers.

UK prospects and potential

Quantifying the exploitable amount of shale gas reserves within the UK is challenging, but in May 2012, Dart Energy International reported a best estimate of shale gas reserves onshore of 66 trillion cubic feet.

The Institute of Directors ("**IoD**") conservatively predicts that the country's onshore shale gas reserves would provide enough energy to meet 10% of the UK's gas demand for the next 103 years whilst the Financial Times predicts that shale gas could account for a quarter of UK consumption in 20 years. Increased shale production could also help offset the projected fall in conventional UK North Sea gas production over the next 10 years (which is estimated to equal 13 million tonnes of oil equivalent). The Financial Times has estimated that production of shale gas could reach 2,100m standard cubic feet a day by 2029, which is just over half the North Sea gas production levels this year.

Benefits

The use of shale gas reserves also has wider reaching benefits on both the economy and the environment.

A recent article in the Financial Times predicts that shale gas could bring £95 billion of investment into the UK.

In March 2012, The Independent reported Lord Browne, the former BP chief executive, as predicting that the UK shale gas industry could create 50,000 jobs across the UK. The IoD has predicted a slightly more conservative figure of 35,000 new jobs across the UK.

Gas emissions contain half as much carbon dioxide as coal emissions, so increasing the UK's gas based energy supply would help to save up to 45 million tonnes of carbon dioxide annually, which is equivalent to 8% of the UK's annual carbon emissions.

Natural gas emissions contain fewer particulates and other pollutants than coal and diesel. The IoD anticipate that using natural gas instead of coal for the generation of electricity and switching vehicles from diesel to natural gas could reduce the number of deaths from poor air quality in the UK.

Risks

The use of shale gas as an energy resource is highly controversial due to some of the risks involved in the fracking process. The main risks are water contamination, tectonic plate movements and methane and other greenhouse gas emissions. The European Union is currently considering a legislative framework to manage these risks.

The future

The Government has said that gas *"will continue to be an important part of the UK energy mix"* as a successful UK shale gas industry *"has the potential to create jobs and support UK energy security, benefitting the economy and taxpayers"*. The Government's aim is that a targeted tax regime will unlock investment which will *"stimulate investment and production that would otherwise not have gone ahead"*. The House of Commons Select Committee is due to publish a report on Shale Gas and has been asking for written evidence on the following areas:

- estimates on the reserves of shale gas in the UK, Europe and globally, and what proportion of those reserves are recoverable;
- the reasons why estimates for shale gas reserves are changeable;
- the prospects of offshore shale gas reserves in the UK Continental Shelf;
- whether the UK should consider setting up a wealth fund with the tax review from shale gas;
- the effects of shale gas on the liquefied natural gas industry;
- whether shale gas could lead to the emergence of a single, global gas market;
- effects on investment in lower-carbon energy technologies; and
- the potential impact on climate change objectives with a larger use of shale gas.

In May 2011, the House of Commons Energy and Climate Change Committee produced a report on shale gas which recommended that the UK Government monitors the regulatory approach taken in Poland and other EU countries where shale gas is explored and produced. In this report, the Committee acknowledges that the offshore shale gas reserves could be far greater than the onshore supplies. The Committee therefore recommended that the DECC encourages the development of the offshore shale gas industry in the UK.

In a press release on 8 October 2012, the Treasury said that the Government will interact with companies to ensure that tax regime is *"appropriately targeted while maintaining a fair return for the Exchequer"*. Ed Davey, Secretary of State for Energy and Climate Change, has since confirmed that he hopes to be able to *"give the green light"* to fracking around the time of the Government's gas strategy announcement, which is expected in early November. With these announcements, the UK, in future, will be better placed to take advantage of the opportunity to develop a cheap and reliable energy source which will reduce the country's dependence on foreign gas imports.

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