Your World First

CMS Law.Tax

OGA and Regulatory Reform

'Business as usual' is not enough

The Oil and Gas Authority (OGA) became an executive agency of the UK government's Department of Energy and Climate Change (DECC) as of 1 April 2015 and should be fully established as a 'GovCo' by this time next year. As the operationally independent, Aberdeen-based regulator of the oil and gas industry, OGA is tasked with implementing the UK's strategy to maximise recovery of the remaining UK Continental Shelf reserves ('MER UK'). In doing so, OGA has already made clear that it expects a culture shift within industry to a collaborative approach throughout the contract chain. Over the next few years, 'business as usual' is likely to look very different.

The impact of OGA's role on the industry as a whole will depend in part upon the final MER UK Strategy which the Secretary of State is required to produce in terms of the Infrastructure Act 2015, setting out how the principal objective of MER UK is to be met. The MER UK Strategy will be a crucial document that commits the OGA, the Government and Industry to work together collaboratively to optimise MER UK for the good of the UK as a whole Preparation of the Strategy remains a work in progress - drafting work is underway with the help of industry stakeholders, with the intent of finalising the Strategy as soon as possible, and certainly ahead of the statutory deadline of 12 April 2016. Once finalised, the Strategy should provide the industry with a starting point for moving forward, evaluating what is required and implementing those actions.

Meantime, to assist OGA in achieving its aims, the UK government has proposed that OGA should have a more extensive 'toolkit' of powers than any of its predecessors to call upon where companies do not comply with the terms of their licences or with MER UK. The recent release of the draft Energy Bill, which was put before the House of Lords on 9 July 2015, underlines that intention.

Sanctions – the 'stick'

OGA will have a broad range of sanctions available to it. At the 'lower' end of the scale, these include enforcement notices, detailing the measures which OGA consider necessary to remedy non-compliance, and imposition of a financial penalty of up to £1million (with discretion to increase this up to £5million). In more serious cases, ultimately OGA will have the power to issue operator removal notices or revoke licences where necessary.

It is hoped that this new regime of sanctions to punish infringements of MER and licence obligations will allow a proportionate approach from the regulator, providing

flexibility to ensure that sanctions imposed are appropriate in each circumstance. Although OGA is tasked with providing some guidance as to how it will exercise its powers, only over time will we be able to tell how effective this 'tool kit' is in practice. OGA's initial decisions may be particularly important in setting the tone, as it will want to avoid a situation whereby companies pay 'lip service' to MER UK, in the knowledge that they will face insignificant sanctions as a result of non-compliance. The proposed maximum fine is perhaps not particularly substantial given the sums regularly encountered in the industry, and some may question whether such sanctions will be sufficient to ensure compliance. However, even a relatively low-level fine may act as a worthwhile deterrent, as operators are likely to seek to avoid establishing a track record of sanctions and consequent potential reputational and commercial damage. And, of course, OGA will also have a range of more serious sanctions (ultimately licence revocation) available to it if circumstances require.

'The carrot'

However, OGA's new powers are not limited to imposing sanctions, and initial indications are that OGA's preference will be to use a 'carrot' rather than a 'stick' in encouraging companies to embrace the new collaborative approach to business. To that end, OGA will have extensive rights to be given notice of and to attend key meetings as an observer, for example where matters impacting licence obligations or the MER UK Strategy are to be discussed. It will also have access to data and other information in order for it to monitor the progress of individual fields. Indeed, the Energy Bill as currently drafted appears to place an extensive obligation on companies involved in such meetings to provide OGA with advance notice of such meetings including providing agendas and papers. The hope will be that OGA's involvement at such meetings will have the effect of moderating the approach taken by parties and so limit the adoption of unreasonable negotiating positions in turn giving rise to more protracted disputes or delays. However, in practice, OGA's involvement will likely be limited simply by the extent of its available resources and so OGA may have to choose carefully which meetings it attends in order to have greatest impact.

Resolving disputes

The creation of OGA as a 'proactive' regulator may also impact the way that that industry disputes are dealt with. A reduction in the number of commercial disputes delaying projects and readily available third party access to infrastructure on reasonable commercial terms have been highlighted as of particular significance to the continued commercial success of the UKCS as a mature basin. Under the Energy Bill, OGA will also take over from DECC responsibility for dealing with disputes regarding third party access to infrastructure, and will have power to provide recommendations to resolve disputes relevant to MER UK or to activities under an offshore petroleum licence. It will have a broad discretion as to which disputes that it will accept and as to the steps that it may take in relation to those which it does agree to entertain. Disputes (at least as regards access to infrastructure) are arising more frequently, as parties discover that arrangements negotiated ten or twenty years ago are no longer commercially adequate against the costs of maintaining and operating increasingly aging assets, and so this has potential to become a significant area of OGA's activities.

OGA has confirmed that for now it will continue to use DECC's guidance in relation to accepting and handling third party access disputes, but that it will review the guidance in the light of industry comments, experience and other information when necessary. It will be interesting to see whether OGA's approach changes once it is in a position to properly assess the effectiveness (or otherwise) of the current approach. For example, DECC's approach to date has been to try to encourage parties to reach an agreement, with determinations rarely being issued and only very limited details of particular disputes being made available. It remains to be seen to what extent OGA will take a similar approach and how any decisions or recommendations it makes will be publicised or enforced.

Industry has been watching the establishment of the OGA and its initial steps very closely – it is likely to watch even more closely as OGA develops its approach and starts to exercise its powers once the Energy Bill comes into force. Companies will be keen to understand how OGA will approach the various aspects of its role on a day to day basis, and will look for transparency, certainty and consistency in the exercise of its powers. What already does seem certain, however, is that the on-going regulatory reform which has led to the establishment of OGA with its central focus on MER UK, will necessitate a considerable change in culture for the oil and gas industry in most aspects of business life.

This is the latest Foresight article in our Transformation series looking at the future of North Sea Oil and Gas. Discussing various issues from technology to employment and disputes, our sector experts offer their commercial opinions on the future of the industry. Please feel free to forward this Foresight to a colleague or to subscribe to our mailing list here CMSEmployment.Team@cms-cmck.com.

Key contact

Valerie Allan
Partner
T +44 1224 26 7149
E valerie.allan@cms-cmck.com

1508-000015-2