

The Select Committee on the European Union

External Affairs Sub-Committee

Corrected oral evidence: Brexit: Future trade between the UK and the EU in goods

Thursday 27 October 2016

11.15 am

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Members present: Baroness Verma (Chairman); Baroness Armstrong of Hill Top; Baroness Brown of Cambridge; Lord Dubs; Lord Risby; Lord Stirrup; and Baroness Suttie.

Evidence Session No. 4

Heard in Public

Questions 48-63

Witnesses

I: Mr Chris Hunt, Director General, UK Petroleum Industry Association; Mr Michael Tholen, Director of Upstream Policy, Oil and Gas UK.

Examination of witnesses

Mr Chris Hunt and Mr Michael Tholen.

Q48 **The Chairman:** Ladies and gentlemen, we will go on to our second session and welcome our guests, Mr Tholen and Mr Hunt. Thank you very much for coming in this morning. This evidence session is in public and it will be broadcast. There will be a transcript, which will be sent to you after the session so that, if any corrections need to be made, there will be an opportunity for you to do so.

We will put a number of questions to you. You will have had sight of those questions; however, we recognise from this morning's session that the Committee may decide to come to you with different questions to the ones that you have seen. I would ask you both to give us a view of your short-term and long-term vision of post-Brexit when responding to the questions, if you can.

Perhaps I may start off by asking for your overview of the importance of trade with the EU to your industry. Especially given the international nature of your sector, the destination of exports can be changed relatively easily, but how easily can imports be sourced from alternative countries?

Michael Tholen: Thank you, Lord Chairman. Oil & Gas UK is a trade association which has many members within it. There are 400-plus and we cover the whole range of activities from oil and gas production around the UK to providing goods and services, both to our own market in the UK and to 100 countries internationally. For us, clearly, the ability to trade freely and openly with Europe as part of a much bigger picture is vital. We rely on investment from Europe. We rely on goods and services from Europe and we provide the same to the European oil and gas market, both to service opportunities in Europe and to work with them on international opportunities outside our own continent, so the ability to sustain trade globally is vital for us. We need to work together on those things, as we do now, in the years to come.

Chris Hunt: Let me first say thank you to the Committee for the invite. We in the downstream industry very much value it, as it helps our visibility. It was notable that the Secretary of State for Exiting the EU omitted us from the roundtable discussions on energy, which we think was a vast oversight. We seem to be pretty much invisible in the downstream oil industry, even though we are the ones who keep the country running, flying and so on. UKPIA represents the eight major refining and marketing companies for downstream oil in the UK. We are responsible for more than 85% of all inland fuel demand. We operate all six UK refineries, which account for the fourth largest refining capacity in the EU. They also account for 33% of UK primary energy and 88,000 jobs depend upon us, through 36 distribution terminals and 1,500 miles of pipeline.

With no disrespect to my learned colleague here, I would just state that crude oil is wonderful stuff but it is absolutely useless unless you refine it into products that the consumer can actually use. So post-Brexit, we would say that it is absolutely vital to have a good, indigenous UK refining industry. This industry is vital to us and we are as interested in what comes of the industrial strategy as what comes of Brexit negotiations. We think that an industrial strategy would be wonderful. We would like one but have never seen one, and we would like to be included in it.

The importance of trade with the EU is that as a nation we currently export about 20 million tonnes of refined products and import about 30 million tonnes, so there is a balance on imports that is kind of traditional. It is driven by some Europe-wide differences in the supply/demand balance. The demand balance in Europe has been swung very much towards diesel, as I am sure you are aware—for instance, through fiscal measures and duty differentials. At the refinery, you cannot manufacture everything that you would like from a barrel of oil. You cannot say that you will make all petrol one day and all diesel the next. You are pretty fixed in what you can do and we cannot make enough diesel in Europe. We therefore import about 50% of our diesel requirement from a wonderfully stable place called Russia, and about 60% of our aviation fuel from another wonderfully robust place called the Middle East. That accounts for the difference.

The balance overall with Europe is about equal; it is about 15 million tonnes in and out. If there were tariffs which affected that, those balances might shift, but as there have been no published tariffs so far—none at the moment—we cannot really comment on how that might go. We would say, though, that in terms of the basic crude that we import, 52% of our crude comes from the North Sea. But surprisingly, 40% is from the Norwegian fields and 12% from the UKCS.

For us, the key thing on the whole Brexit negotiation is to have adequate collaboration with industry in all the discussions, because there are serious things to be talked about during Brexit. We ask for stability. In our opinion, we cannot see how on earth we can unravel the 300-plus bits of European regulation that we are currently bound by within the time after the firing of Article 50. We therefore envisage that there should be a mass transfer of regulation to start with; we can then do the laborious bit of unpicking it at some later stage. By and large, we are on board with the majority of EU regulation that we have signed up to as a nation, although we might have some quibbles with how it is implemented in the UK.

Lastly, I think it is critical to us, in both sectors of the industry, to have access to markets and people. We move between 1,000 and 1,500 people from the UK into Europe and back again each year. There are around 82 locations throughout Europe which are affiliated to UKPIA members and where they have offices and plants. We move highly skilled people

around through the processing we do, which is highly technical, so that is key to us. I am sorry if that was a bit long-winded.

- Q49 **The Chairman:** No, that has been extremely helpful. Just to follow on from that, particularly on the Continental Shelf and the investment decisions that are needed over the short and the long term there, it would be useful to have your own view on your responses to scoping for different scenarios.

Chris Hunt: To address that from the upstream, in our decision-making progress, which has been brought into really sharp focus post-Brexit, there are a number of things that we have to bear in mind. The ability to see investments through—they typically last for 20 to 25 years—means that people have to understand the fiscal, regulatory and business environments in the years to come. The uncertainty that Brexit delivers for us is for things such as our ability to understand how the European Union will influence policies that may be applied in Britain after Brexit and our ability to access a skills base, that is both international and from across Europe, to service our industry and our opportunities in the North Sea.

Coupled with that is any uncertainty about investment, since we sit at a time when investment is falling. Two years ago it was at £15 billion; that has fallen down to £9 billion of ongoing investment. But now new investment is at a real low of less than £1 billion a year, because our industry is obviously very constrained in the current business environment. Anything meaning that investment is tight and investor sentiment is uncertain about the opportunities in UK markets preferentially advantages other opportunities outside Europe.

- Q50 **Lord Stirrup:** Can I return to the issue of tariffs, which Mr Hunt mentioned briefly? What would be the effect on the sector of the imposition of various tariff barriers between the UK and the EU, and how would it affect the supply chain—for example, the export of downstream products? What about rules of origin? What sort of impact would they have if there were some constraint there? In outlining the impact of various possible outcomes, will you also say how these could be overcome, apart obviously from not having them in the first place, which we all understand? What ways are there of working around these issues to overcome the problems of timeliness of supply and so on?

Chris Hunt: Looking at it from a downstream perspective, our exports depend on trading agreements and market demand. As I said, if we look at our export/import with the EU, there are around 15 million tonnes each way, so in theory you could say that if that stops, so be it. At present, we have no published or proposed schedule of tariffs, but one would hope that if tariffs were imposed they would be reciprocal, so that would affect exports as well as imports. From a global business perspective, we would need to see how that panned out.

The other impact of tariffs is on equipment—spares and so on—which, again, we would need to follow very closely. That would have an add-on

effect if it is one-way, depending on what our national export capability is. The barrier-free movement of goods and people is very important to us, as is inward investment. One of your questions was about inward investment from the European bank. We are focused in the downstream industry on making the UK downstream refining sector attractive to corporates to invest in. The biggest barrier for us in that respect, even from the European refining respect, has been the fact that we trade in an international market—we are global traders—and we are subject to imports from countries that are not subject to the same regulatory regimes as we have in the UK and Europe.

For us that is the biggest issue, because in terms of price and the cost of our manufacturing that puts us at a disadvantage versus, for example, the countries where the big investment is going—the Middle East and India. At the moment, we can import freely from those countries and they are not subject to those costs. So we need a regulatory framework that is stable and predictable, and fiscal policy that is long term, because, like upstream, our investments are long term. We are looking at 15 or 20-year horizons for investment, and it is significant. We have over £40 billion invested in fixed assets and we invest something like £3 billion a year. An awful lot of that at the moment is just on compliance with environmental regulation. I am not saying that we should do away with that, but we have to take a pragmatic view as a nation on how we treat our manufacturing industries in the UK, and how that responds to outside influences.

As a final example, if you substitute 100 units of manufacture from a UK refinery with 100 units of manufacture from a refinery outside the EU, there is a 35% CO₂ penalty in bringing that product in, due to the relative inefficiencies of those areas; so I think it is in the nation's interests to look after indigenous production.

Q51 **Baroness Brown of Cambridge:** I would like to explore the importance of EU rules and standards and our compliance with them for both our trade within the EU but also away from it. Are they valid as international standards? Are they important for us outside the EU and, indeed, would we be interested in wanting to stick to them or are there benefits from being able to depart from them?

Chris Hunt: I think we have slightly different takes on this, but from a downstream point of view, most of our technical standards come under two areas. One, as you would expect, is fuels and fuels quality, lubricants and so on. Those technical standards come via a group called CEN [the European Committee for Standardisation], which is a European body. But CEN is open to non-EU members. That is where we send our experts. There are experts from British Standards and from the industry.

Baroness Brown of Cambridge: I understand that it would make no difference.

Chris Hunt: It should make no difference. That area is free of politics. There are also international standards, as you would expect, particularly

appertaining to aviation and marine products, which are global. The British Standards Institution (BSI) will maintain its role in maintaining those standards, as now. On safety, we would obviously be very keen to ensure that we stick with the Control of Major Accident Hazards (COMAH) regulations controlling major accidents and hazards that came out of the Seveso III directive. We would want to see that encouraged and maintained, so for the downstream industry we do not see a vast change. We will still retain our influence and power there.

Michael Tholen: Thank you, Mr Hunt. On the upstream, standards affect our business in some rather different ways because of the quality of output, which is probably one of the things that determines standards within the refining industry. So they are translated rather differently in our business. As an industry we are in many ways the thought leaders and activity leaders on safety and, indeed, on environmental performance standards across Europe. The EU has no direct remit over the precise activities of oil and gas extraction offshore. That said, it influences our industry in two ways; one is through environmental standards, and the second is through the standards upheld within the energy market within Europe.

One example is gas quality, where for many years we have had a gas quality regime that comes from the British Gas days, with specific technical specifications. There is a desire to create a unified natural gas specification across Europe. That is something that we are negotiating on as a country with the EU through BEIS and which, if it were implemented currently, would actually restrict production in the UK of both our own stuff and imports by about 20%, so the gas market would be in deficit by 20% of supply. While we remain in Europe, you can influence those things and negotiate and come to a unified standard that works both for those producing and for those transmitting gas in good quantities across borders. At the moment we import roughly half our gas demand in the UK for instance, yet at the same time we also export about 10% of our production. So we are part of a much bigger European energy market and the standards applied there. How they apply to us post-Brexit will have an influence on our own energy market and, indeed, back into the European market.

Baroness Brown of Cambridge: I am hearing that downstream it is not a particular issue, but upstream it is.

Michael Tholen: For the upstream industry it is much more subtle and pernicious in some ways. The ability to influence those standards in a positive way post-Brexit for a very interrelated and complicated energy market will be vital.

Baroness Brown of Cambridge: And the upstream point is different. It is not just that anybody can come and join. There is a definite EU oversight.

Michael Tholen: It depends on the nature of the separation of the upstream market post-Brexit from the European market and any lack of

clarity on how energy policy and the UK's own energy policy will emerge in that new world. When you sit as part of a common energy market, there is free movement of electricity and gas. There is much less for oil, because that ends up in refineries and is sorted out at a local level. Then the ability to have fungible products and free open markets, which the UK has championed, will be vital.

Baroness Brown of Cambridge: Would we not be able to retain a seat at that table because of our background, skills and contribution in that area? Would they not want us to contribute?

Michael Tholen: I would like to think so, but I think we need the clarity from government on its intent. In conversation with colleagues in Norway, who clearly sit at a different place at the table, there is a great degree of soft influence. But even there there is a large measure of frustration about the ability to influence specifics, which ends up otherwise making the market more difficult to access and free movements of energy harder to achieve for providers and consumers.

Baroness Brown of Cambridge: Would not Norway not be a powerful ally on that?

Michael Tholen: I like to think so, yes. But even within Europe, some of the current producing countries have expressed some private regret that we are no longer likely to be able to speak as loudly for an industry which is a very responsible and active one in Europe, when we are on the other side of the table.

Q52 **The Chairman:** Before we move on to the next question, could I have your view on the capacity markets that were introduced? What impact will Brexit have on us in our position in the UK, making sure that the capacity that we are buying in from Europe is not negatively impacted?

Michael Tholen: It is not an area where I have had much input from members on their concerns. The trading in capacity—if you are thinking about gas capacity—is mostly done within the UK and the national balancing point. As gas markets emerge, we will have to see our relationship changes with other gas markets, which could influence such things as gas storage and access to the European gas storage market rather than just the UK market post-Brexit.

Q53 **Lord Dubs:** Are there other areas of the EU legal regime that have a large impact on trade by the sector—for example, steel tariffs or the broad energy policy? Will leaving the EU advantage the sector in this regard or will decisions made by the EU continue to have an impact on the sector's ability to trade?

Michael Tholen: Perhaps I can pick that up first from the upstream perspective. Clearly, we will have to see how European law is translated into British law, post-Brexit. With the assumption that what is now remains in years to come, at least initially, we will actively comply with environmental law. That is probably the biggest single area in which it will have an impact on the offshore industry. With things such as the

Emissions Trading Scheme, which we clearly want to continue to comply with, the ability to engage and see how that policy formation changes as we move to the next phase in the scheme will be of great interest to the industry. It is part of shaping and engaging our policy in the light of an Emissions Trading Scheme which is not specifically directed at our industry but has big implications for it, and how that emerges if you are less able to influence those policies that then translate into law.

Chris Hunt: For the downstream industry it is very similar. It really depends on how we shape our future relationship with the EU on environmental law. The EU ETS phase 4 is at a pretty critical stage of negotiation, and the UK was leading that discussion—in fact, the rapporteur was a UK MEP. That will be key. There are lots of interesting discussions to be had, as they say in politics, on how we go with that—whether we have a parallel scheme, are in that scheme or develop our own scheme, which has very big implications for any number of energy-intensive sectors. But there are other parts of the EU legal set-up for environment, safety and REACH—the whole area of registration of chemicals is another big one—which it is very difficult to see how we could unravel, even if we wanted to, even though it is a monstrous and huge set up. But we want to keep selling products to the EU, and we must therefore comply with rules and regulations. Where we go as a nation with our forward thinking on the relationship with the EU on environmental regulations will be pretty key. I hope that there will be a lot of discussion and collaboration on that area.

The Chairman: But there must already be scoping going on with the sector, given that there are several scenarios, and you must be scoping for each scenario.

Chris Hunt: Yes, we are looking at the various scenarios, but it is a question of how much resource and effort we can put into that without having a clear understanding of where government wants to go. Our clear understanding is that there is no great willingness within government to want to decouple totally from where we have been for the past 10 or 15 years on environmental policy. Neither would we, from a business point of view, expect any dramatic change, or want one, from where we have been on policy. It is more to do with the nuances around where we take EU ETS forward. We would need some sort of emissions trading scheme in the UK, whether that is directly in the EU ETS, or whether it is a mimic, a parallel, or our own scheme. You can look at those options and say that it is more likely that we will be either in or parallel. From a business continuity perspective, that is good. But around the edges of EU ETS, the interesting discussions are those on what you do on the balance of allowances, balancing across sectors and so on. That is where the interesting discussions will be.

Lord Dubs: If I can follow this up, would not full compliance be in our interests, unless there is some overwhelmingly powerful argument that we should not fully comply? As a general proposition, should we not fully comply, and say to the Government that that is the best place for us to

be?

Chris Hunt: As I said, even if Brexit had not occurred, there are and will continue to be discussions between industry and our regulators and negotiators on where we would like to be in terms of the EU ETS phase 4. Certainly, there is general support for an Emissions Trading Scheme; that goes without saying, from our sector. But the interesting discussions, because there will be severe impacts around those discussions, are on the fringes—about levels of allowances, whether there is going to be a tiered scheme and, if so, how it will operate, and so on. That is where I would hope that we would have some good and interesting discussions.

Michael Tholen: Perhaps I could build on that. There is a need for clarity post-Brexit from the new Department for Business, Energy and Industrial Strategy on a whole range of factors, not just the translation of current rules into UK law but on energy policy within a UK context, as well as industrial strategy. Those are vital elements for that continuing of business in the UK. We sit with the assumption that some rules of the game will continue to apply—and I think that in great measure that is likely to be the case. But the stronger and clearer the signals on things like energy policy and industrial strategy, rather than keeping them as titles simply for the department, the clearer the confidence in investment, not just for our own industries but for many other industries that are trying to work out how to operate in a future uncertain environment.

Q54 **Lord Risby:** I turn to the area of energy services. I have some contact with Algeria. Part of our commercial energy relationship with Algeria is a very strong service element to its energy industry. Given the importance of some of our companies engaged in this and their excellent reputation, I would like to understand to what extent, on the energy service front, how quantitatively exports to or activities in the European Union compare with those outside. Are there any lessons to be drawn from this?

Michael Tholen: Perhaps I could take an example first from upstream here on the provision of integrated services. Globally, our exports of goods and services were something like £16 billion in 2014. Clearly, there is a range of services and goods in what we do, many of which are integrated at that point of need. For many countries, you have to locate that source where there are the least barriers to get access to the demand for those services, because they are often needed urgently to solve specific issues. Within the current European market we have a great ability to move goods and services directly and immediately around Europe, and we have great infrastructure. The issue for our member companies is the impact on that flexibility if new and otherwise undesired barriers, be they in VAT and the like or the customs union, start to provide friction in transactions. That may mean that companies will need to relocate their goods and services supply into the mainland European market. Those sorts of things are more likely within a European context, which may lead to subtle or bigger changes to the emergent business environment in years to come.

Chris Hunt: Downstream, there is a fair degree of interrelationship between UK refineries and their sister refineries in Europe in the transfer of part-processed and processed products. That operates extremely well in optimising production capability across Europe; you can transfer parts to another refinery, which has a better capability in that area. There is a particular concern about that. If tariffs and restraints were put on, they would obviously affect that and we would need to adjust. By the way, we are a very good industry at adjusting.

The other side, of course, is the people. As I said previously, we have around 84 locations across Europe where UKPIA have interests in manufacturing and marketing. We move people with skills around, such as highly-skilled refinery technicians. As you are talking about services, I also put in a plea, because about every six years each refinery has to have a major turnaround, as we call it. At that point, the refinery will partially or completely close and a whole host of maintenance and repair goes on. At that time, there will be something like 1,200 contractors on a refinery site in addition to its normal employed staff of 500. Some of those contractors will be highly specialised groups that come in to carry out maintenance and installation on specifically licensed bits of production. In other words you cannot just say, "We can do without them and employ folks from the labour exchange". You need the folks who are highly skilled in that area. The concern for us is the ability to move highly technical staff around and about getting access to these highly skilled maintenance people—and likewise, our highly skilled folks who go to refinery sites abroad.

Q55 **Baroness Brown of Cambridge:** In relation to oilfield services, is the implication that we would lose oilfield service companies such as Schlumberger, because there would be no advantage for them to stay in the UK? Could it also inhibit growth in using the skills that we have in Aberdeen that support the offshore wind industry, for example, which at the moment is a real possibility for us because we have such a good installed base now? Do you think that we would then struggle to apply that in the rest of Europe?

Michael Tholen: Inevitably, you are trying to see what may emerge in years to come in the market that you would then play into. Some of the bigger oilfield services companies have already done a lot actively to rationalise their businesses because of the nature of the industry and where it is at. They have worked on the basis that they have services and service supplies coming from the UK, the Netherlands and other parts of Europe to service the UK market. There will clearly be two sides: one is that additional barriers may make them less willing to provide those services to us in the first place if our own industry diminishes in size, which is why sustaining investment through the cycle is vital. On top of that, their ability to access other markets where there may be growing demand will be important as well.

I was reflecting a little on where the emerging oil and gas markets are within Europe, which is interesting. Taking an offshore perspective, they are in the eastern Mediterranean and the Black Sea, offshore of Romania.

They may even be offshore of Ireland, who knows? There is seismic shooting yet again in that area. Given how the emerging oil and gas market changes in years to come, our ability to access it will also be part of the focus of service companies, as it is for the people operating and working out of Aberdeen.

Q56 Lord Dubs: If the UK were to leave the Single Market, would that raise any other practical problems with respect to exporting to or importing from the EU? I am talking about things such as inspections, customs delays or shipment issues. On the other side, would it give us any opportunities at all?

Chris Hunt: From downstream, Lord Dubs, because of the nature of our products we are fully immersed with our dear friends in HM Revenue and Customs on all manner of inspections and checks. With shipments, because of the high value of our products it is also very much in the interests of the companies involved to take the outmost care and scrutiny of volumes delivered and of quality and so on. However, I would say that any additional red tape, and the forms involved, would be unwelcome and unhelpful. They always tend to be expensive and to have a number of audiences who want them expressed in different ways, as we have found with other regimes. I do not see an immediate additional opportunity.

On the imposition of extensive tariff reporting inspections and customs over and above where we are now, bearing in mind that we have an awful lot of them the moment, it is certainly hard to see that really happening in our case.

Michael Tholen: From the upstream sector, the main focus would then be on the provision of goods and services—servicing our offshore market and the European offshore market. The Union Customs Code, which came in earlier this year, has been something that companies are taking time to accommodate. It has led to some new administrative burden, but there are other freedoms because of it. Clearly, a change in years to come will mean that we have to transition to something new. But the ability to access the Single Market with the least friction possible—it is for us to choose how that solution comes about—will be vital to make trading as efficient as it can be when we are cleared to access those opportunities from the UK perspective.

Chris Hunt: If I could add one point, at the moment the import or use of goods for processing—we are talking about crude oil or part-finished products—is tariff free. Our expectation of HMRC is certainly that, post-Brexit, we would like it to continue with that. It will otherwise become a major hassle for downstream refining.

Q57 Lord StIRRUP: Can I return to the issue of investment? I think Mr Hunt said earlier that as far as the downstream part of the business is concerned, the focus is perhaps rather more on investment by corporates than by Governments. The availability of investment from Governments, for instance through the European Investment Bank, has been cited as a major issue for the industry, particularly with regard to exploration and

infrastructure. What effect is Brexit likely to have on all this, and if it is bad, how might that be overcome? What can be done to mitigate the effects and retain investor confidence in the long term?

Michael Tholen: Maybe from an upstream perspective, the big drivers on investment are clear on the opportunities you are looking at with regard to the reserves and the resources offshore and the cost base and skills base to do that. In the current market we have seen a huge change so that costs have fallen by nearly half to pursue some of these opportunities in the last two years. We have seen big fiscal and regulatory changes which are designed to help that investment and which should do so if sustained at the current competitive place for a long term, so we sit in a better place than in the past. At a time when the industry is clearly constrained for capital, because there is little free cash within the industry when we have such low oil prices, the competitive nature of this market against other markets is taken into account.

It comes back to uncertainty about the inserting of regulations and uncertainty in the relationship with Europe, which are a subtle rather than explicit factor in where we make decisions. There are many more subtle things, and investment is often an emotional thing from the private sector, which is brought to bear. Therefore the ability to allow the right skills to access those opportunities and to appraise those investments sufficiently, along with, as my colleague Mr Hunt mentioned, the movement of technical skills through and across the market to make sure that we use the best brains to access those opportunities, will be vital. Within a broader European context, things such as developing Aberdeen as an oil and gas hub are mostly being funded very supportively by the UK and Scottish Governments, and we hope that that will continue in years to come, even post-Brexit.

Chris Hunt: I reiterate that if we look at the downstream oil market, demand is effectively static or likely to decline slightly; we are in a market where the demand and supply are completely out of balance because of the fiscal move towards stuff like diesel. We are in a market where, compared to our global competitors, we have very high energy costs, relatively high labour costs and, certainly, the highest regulatory cost burden globally. Those are the views from corporates which have the opportunity in the downstream industry to invest anywhere in the globe, particularly in emerging markets in Asia, the Middle East and Africa, and so on. That is the pond in which we fish. Particularly now that these corporates are looking at the UK and saying, "What on earth is going to happen with Brexit—is this a place I want to invest in, with all those factors we already have, plus Brexit?", it would really be helpful if for once we had an industrial strategy that truly looked at manufacturing and valued it. If you take as an example the recent relative debacle around steel and the steel industry, we would like an industrial policy that looks long term and sees where it values manufacturing; we should not avoid environmental policy or other policies that incur costs but we should look seriously at how they are placed upon the manufacturing industry in the

UK and give some good long-term signals to potential investors. That would help enormously towards a post-Brexit world.

Q58 **Lord Stirrup:** I will follow that up with a question, which is perhaps slightly from left field. So far today we have not mentioned fracking. Were the Government to embrace a substantial extension of fracking throughout the UK, would that affect the answers you have given so far in any regard? Would it be Brexit-neutral, would it create more difficulties for it or would it make it easier? I am at a loss to understand.

Michael Tholen: Maybe I could take that question. Our industry has used fracking as a technology for many years offshore and to good effect. It is part of the toolkit you need to use to access and maximise recovery from resources. Clearly, onshore within the UK energy policy and regulatory policy, which are creating an opportunity to access the UK's onshore and gas resources, are still changing, and we may find that those continue to diverge from Europe post-Brexit. Again, coming back to my earlier position, the clarity of energy policy and the certainty around it for the UK post-Brexit will help to provide a framework for companies to decide how to invest responsibly and maybe to deploy that technology within a UK context. Clearly, clarity and certainty, and having a strong, reasonably regulatory oversight to demonstrate the compliance and efficacy of that technology, will be vital.

Chris Hunt: I would merely say that UKPIA does not speak for the fracking sector. It has its own particular trade association. However, I point to what has happened in the US. For us, that was one of the main markets for Europe to market its excess petrol, as the US, as I am sure everyone is aware, is mainly a petrol-using country. Within a period of about six to eight years, the fracking sector in the States has made it virtually self-sufficient in that fuel, so it has enormous benefits on that side, for one thing. It has also had enormous benefits for the US refining industry in the provision of what we would class as interim products for refining. Therefore without delving too much into the rights and wrongs of fracking, which is entirely a matter for policy, you can see the benefits of fracking and what it can bring by looking at what has happened in the States. I hope that we get some clarity on that shortly with a long-term energy strategy that includes downstream and upstream oil as well. Fossil fuels still have so much to offer, and as every long-term energy demand scenario has said, over 80% to 90% of all transport fuels will still be fossil fuel-derived in 2030 and beyond, so we are very much needed and should be listened to carefully.

Q59 **Baroness Suttie:** Can you say a little about the impact that the depreciation of the pound is having on your industry?

Michael Tholen: I will first speak from an offshore perspective. Over the years we have seen many exchange rates, so this is quite a remarkable low point in the cycle, depending on your perspective. For those producing oil and gas in the first place, specifically oil, it has a slightly unusual context as the price of their product in pounds has risen, or their cost in dollars has reduced—you can slice it either way on those things.

Therefore it has gently had an improving effect on the UK's competitiveness and has helped a little from a producer's point of view. Clearly, for society, we all know the discomfort people have as oil prices go up at the petrol pump, so it is clearly not a common good for everyone in the same way. Across the broader supply chain, where many of the goods and services are often priced internationally in dollars, the benefit you see is probably less effective because again, many of the input costs come from abroad to goods we then export. Therefore there is a subtle benefit, but there is uncertainty as to whether that offers a long-term advantage for the industry.

Chris Hunt: Downstream, we are well versed in the perils and pitfalls of exchange rates, as is reported more or less weekly in the *Daily Mail*—according to that we are always robbing the consumer by what we do to petrol prices. Fluctuations in dollar rate are our bread and butter, and we tend to ride on those changes in exchange rate. To give you some indication, all our crude oil is obviously dollar-based, as is the export and import of the finished product. A \$2 a barrel change in price roughly equates to about 1p a litre. So, as Mike said, the effect on the consumer is pretty drastic. But most of the refining costs in the UK are sterling-based, so we are a bit immune from that. Changes in exchange rates are something we are well versed in, unfortunately.

Q60 **The Chairman:** Thank you. How important to you is continued or equivalent access to the EU's free trade agreements with third countries, and what are the particular barriers to trade that you feel the Government should be tackling in these agreements?

Michael Tholen: From an upstream perspective, at the very least we would like to see a continuance of the arrangements by which companies can access the main markets from their position in the UK. Certainly the most recent figures that I have say that well over 100 countries are accessed by goods and services from our own members within the UK. So clearly it is a wholly international market and one that you want to become only more, rather than less, attractive in the years ahead. Therefore, at least stability and, if there are barriers, the continued ability to make those easier and more accessible would be beneficial. I have not been given anything more specific than that, so I think that I can probably stop at that point.

Chris Hunt: It is essential for us, as the EU and US are key export markets, and we have markets that do not really come under this particular area. I really hope that this is played out in the whole discussion about equivalence and how equivalence works. I hope that we can get through the Brexit negotiations with minimal impact on our goods and services and movement of people—but, until we have a clear idea of what is implied with tariffs and so on, it is difficult to answer.

Q61 **The Chairman:** Since you are already looking at assumptions, through the lens of looking at those assumptions, where would you like the Government first and foremost to consider how to make it easier for your sector to be able to operate post Brexit?

Chris Hunt: There are two ends of that lens. One is more or less the situation as it is now, which is unlikely following the Brexit vote. The other is right at the other end, where you go total WTO. I re-emphasise that it really depends where on that long scale we end up in our discussions. We would prefer to be as far to my left as we can be, which is as near as possible to where we are now, rather than to the other end. But, until we can see something that we can have a good look at and a chew on, I do not know.

The Chairman: I want to press you a little here as yours is a huge industry. What I am trying to gather from your evidence here is whether there is a wider range of thinking on assumptions going forward so that, when we put our report together, we can look at your lens of barriers, from huge ones to smaller ones—but I am not sure that I have drawn that from your response.

Chris Hunt: We have certainly done some provisional work, but I am sure that you understand, Baroness, that this is a huge area to look at. Every time I meet representatives of our Government and ask, “Where are we?”, they say that they are looking at it and gathering evidence. I think that we are in a similar position, where we are starting to say, “What if it went that particular way?” We have looked at the options and what they might mean—but taking that much further would be very much a matter of conjecture.

Obviously, we have expressed preferences for the things that we would like to see, including, as far as possible, the continuation of free access to markets and the free movement of people—moving technical people and so on. But, to be frank, we have not developed that much further. We are now starting to look more at the implications for key bits of regulation, such as the EU ETS phase 4 and so on, and what those effects might be.

Q62 **Baroness Brown of Cambridge:** I would like to ask you both to put yourselves in the position of being our trade negotiators. What are you going to be selling in terms of the UK’s unique strengths? From the perspective of your sector, why do they still desperately need us in their teams?

Chris Hunt: From the perspective of our sector, as I said earlier, we have the fourth-largest refining capacity in Europe, which is quite outstanding. I think that as a sector we are number one in terms of innovation and skills.

Baroness Brown of Cambridge: Would that be recognised by our European partners?

Chris Hunt: It is part of a European study.

Baroness Brown of Cambridge: Right.

Chris Hunt: We have an industry sector that is extremely innovative, very technical and very highly skilled. There is a lot of innovation in terms of enhancing the process and developing the skills base. I think that that

would be something that they would welcome. We have a long history in the UK of setting tough, stringent and well-thought-through standards in all areas of products and health and safety.

Michael Tholen: From an upstream perspective, our USP as an industry is driven by our technical capability. In many ways, we have led the world in our ability to develop subsea opportunities. That means that, in Aberdeen and in the UK, we are an acknowledged leader in the ability to perform highly technical operations of recovering oil and gas subsea without necessarily using platforms. Within that market, we are also recognised as a thought and policy leader on safety and good operations of facilities throughout their life, which have led to a common European approach to safety. As for the years to come, we are gaining a strong reputation for through-life operation, through to decommissioning late-life operation, in an industry that still has a great opportunity ahead of it in the UK. That sector is developing new skills, which will help us to provide new opportunities in the European market and in accessing globally those competences that we have developed in the UK.

Q63 **Baroness Brown of Cambridge:** We have touched on the fact that there might be obvious allies such as Norway in influencing standards. Are there other obvious partners or allies and are there some strong competitors in the EU who might be pleased to see us depart?

Michael Tholen: From an upstream perspective, clearly those countries that have active offshore oil and gas industries are like-minded about their ability to maximise those opportunities within Europe. It is clear that, within the EU, even Italy and certainly the Netherlands and Denmark feature strongly on the list. We will continue to engage closely with Norway and the focus will be on how we make our case at the table when we sit in a different place. That will be important. The opportunities in the years ahead will depend on our having a coherent and cohesive approach. Many countries within Europe that are perhaps less focused on where the oil and gas come from are in danger of applying rules that fit their local remit in a way that disadvantages oil and gas production in the UK. Were we to remain tightly within all their rules, that would make us less competitive and less able to maximise our hydrocarbon resources, both for our own energy security and to help European energy security.

Chris Hunt: From downstream, we do not tread too much on each other's feet across Europe. The markets tend to be self-contained. Personally, I think that the UK will be sorely missed. What we do as an industry sector in the UK adds to standards and development on safety and innovation. Our political influence in the European Parliament and the Commission shows that the UK has punched above its weight in terms of its expertise and input to the whole process of how the EU has worked. The feedback that I get from my equivalents across Europe is, "You're going to be missed".

Baroness Brown of Cambridge: Do you have a good example of somewhere where our input has been key?

Chris Hunt: I would even take as an example EU ETS phase 4, where the rapporteur was a UK MEP and, my God, he did an outstanding job. Unfortunately, he has had to step down. That was a difficult pen to hold, with so many conflicting views between those who wanted extreme tightening of EU ETS and industry, which wanted as much freedom as possible. He did that in a magnificent way that was respected across the piece, by all MEPs, NGOs and trade associations. That is just one example. I would also give the example of the high regard in which the UK permanent reps were held in Brussels, again for their expertise and for the way in which the UK presents well-thought-through and well-argued information. As I say, we will be missed. Sitting on a European grouping of trade associations for downstream, we certainly made our views clear and always came up with a well-argued case for how we should promote our advocacy.

The Chairman: Thank you very much to both of you for coming this morning. I remind you that the transcripts will be sent to you and, if any corrections need to be made, they will be made on your behalf. Thank you very much indeed. I call this session to a close.