DRAFT

FROM: EUGENE ROONEY
25 JANUARY 2001 **Copy Distribution Below**

PS/FIRST MINISTER
PS/DEPUTY FIRST MINISTER

MEETING WITH THE CHANCELLOR OF THE EXCHEQUER 24 JANUARY – FOLLOW-UP

The First Minister and Deputy First Minister met with the Chancellor on 24 January mainly to discuss the issue of fuel costs in Northern Ireland.

(i) Illicit fuel / Smuggling

The Chancellor suggested that FM/DFM should meet Richard Broadbent, Head of Customs and Excise to discuss the actions which are being taken to tackle the illegal activities. The Chancellor added that Customs resources had been increased very significantly and that some measures had already been taken which have yet to have effect.

There had also been a reduction in duty on ultra low sulphur diesel which taken with the excise duty changes amounted to a reduction equivalent to about 8p per litre. Oil companies should all have moved to using ultra low sulphur fuels by end of March. The Chancellor asked to be informed if this was not the case.

ACTION: Private Offices to arrange meeting with Mr Broadbent

[Note : As preparation for the meeting, officials/advisers might meet separately with representatives of petrol retailers and with local Customs personnel to go through the figures in detail.]

(ii) Vehicle duties for Hauliers

The Chancellor felt that the changes announced in the 2000 Pre-Budget Report (PBR) should have a significant impact on reducing the differential in vehicle excise duties between the UK and ROI. The UK rate for environmentally friendly lorries was amongst the lowest in the EU. Given the different duties for different classes of lorry, comparisons should be made with care. The Chancellor requested that Treasury be provided with any figures which indicated that a significant differential remained in licensing following the PBR measures.

[On agriculture vehicles, Treasury would provide a note on excise duties.]

ACTION: EPU to discuss with DOE

(iii) Climate Change Levy

The Treasury commented that the negotiations over an exemption for NI were more difficult since NI was no longer an Objective 1 region. The case had to be based on environmental rather than regional arguments. The Treasury promised to advise of any developments. In response to a request from FM/DFM for a ten-year exemption period to be considered, the Chancellor noted the request though he felt that this could be difficult to achieve and asked whether there was any incentive to progress on a shorter timescale. More information on this proposal would be helpful.

ACTION: DETI to advise further

(iv) Aggregates Tax

The Treasury felt that there were significant costs in transporting aggregates which operators would need to weigh up against the level of tax. The FM suggested that it would be preferable for such a tax to be applied on a percentage rather than a flat rate basis given the very different average prices across the UK. The Chancellor acknowledged that this option had been considered but that the tax was intended to reflect the impact on the environment. The Chancellor asked for more detailed figures on the NI situation. However, he explained that the general policy was not to give exemptions from a tax to particular areas.

ACTION: DFP to advise on the detailed costings and locations of quarries in relation to the border.

(v) New Deal/ Skills/Young People

The Chancellor was interested in any ideas for addressing skills levels which might be a barrier to future growth and employment creation . There might be a particular focus on training and IT skills for young people. He was keen to increase workplace skills. There were a number of New Deal initiatives already in operation and he would welcome thoughts on the skills issue, particularly for young people, and further development of New Deal.

ACTION: DHFETE to advise

(vi) Viridian Growth Fund

The FM invited the Chancellor to launch the Viridian Fund in Belfast at the end of February. The Chancellor expressed interest and undertook to consider.

ACTION: Subject to Chancellor's confirmation, DETI to prepare

From the inputs requested above, EPU will prepare a response on each of the issues discussed at the meeting for the First Minister's and Deputy First Minister's consideration.

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Annex A

MEETING WITH THE NORTHERN IRELAND FUEL GROUP –LINE TO TAKE

It is recommended that the First Minister and Deputy First Minister use this meeting to:

- Emphasise their continuing concerns at the adverse effects on the local economy of high fuel/transport costs.

- Continue to make the Group aware of the constraints – world oil prices, fuel taxation not a devolved matter and EC constraints - on possible solutions.

- Obtain from the Group an up to date assessment of the difficulties facing different groups and in particular:
    - the views of hauliers on the vehicle excise duty reductions announced in the Pre-Budget Report;
    - an assessment of the effectiveness of Customs' increased anti-smuggling activities; and
    - the latest position on the extent to which illegal activities are infiltrating and impacting on the petrol retail sector.

- Canvas the Group for ideas (in addition to actions by Customs) on how smuggling might be tackled.

- Promise to report back on meeting with Chancellor.

Annex B

FUEL COSTS – Background Brief
(To be used for meetings both with Chancellor and Northern Ireland Fuel Group)

CONTENTS

(a) Discussion of the Issue

1. It will be difficult for the First Minister and Deputy First Minister to produce proposals which are both acceptable to the Chancellor, who will not wish to move from his general stance on fuel and the unitary nature of UK duties, and which meet the demands of the Northern Ireland Fuel Group.

2. Firstly while fuel costs in Northern Ireland are much higher than the RoI, the availability of cheaper fuel from the RoI means that many consumers and businesses in Northern Ireland are much better off than their equivalents in the rest of the UK. No doubt the Chancellor will be aware of this.

3. There are both gainers and losers (see below for details). The main loser is HMT to the tune of around £300m per annum (the RoI Exchequer correspondingly gains around £130m per annum). Petrol retailers are losers though it appears form a report produced by the Legitimate Oil Pressure Group that for some smuggling may have brought significant financial gains. The chief beneficiaries have been the smugglers (including presumably paramilitaries) and it could be argued that the primary adverse impact of the north/south fuel differential has been not so much an economic but a law and order one. ✓

4. Secondly apart from persuading the Chancellor to further reduce fuel excise duties across the UK generally there is little scope for introducing reductions in excise duty specific to Northern Ireland. The EU opposes region specific duty reductions. For example a couple of years ago the EU took infraction proceedings against the Netherlands for offering a retail price subsidy (because of duty differentials) to petrol stations within 20 km of the German border. It was deemed a State Aid and disallowed.

5. There may however be scope for further action on tackling smuggling. In a letter to Sir Reg Empey, Stephens Timms indicated that Customs were implementing an operational strategy involving significantly increased resources to tackle the supply and sale of illicit fuels. He reiterated this message at a subsequent meeting with representatives of the Petrol Retailers Association on 23 October. Scope may remain for further initiatives – for example the Legitimate Oil Pressure Group in a booklet produced in May 2000 on the fuel smuggling advocated the introduction of a tracer dye for all petrol coming into Northern oil terminals.

6. Finally the Northern Ireland Fuel Lobby is a rather disparate group for whom the causes and impacts of high fuel cost can be different. For example farm diesel is exempt from fuel duty and the significant increase in the fuel bill facing farmers in recent years reflects largely the increase in oil prices. For hauliers one of their main grievances is the large differential in vehicles excise duties between the UK and RoI/Continental Europe. Following announcements in the Chancellor's Pre-Budget Report this has been significantly reduced and may well be eliminated for the UK/RoI. While a considerable differential in fuel costs remains, Northern

Ireland hauliers unlike their GB equivalents can access cheaper fuel fairly readily. This helps them to remain competitive vis a vis their RoI competitors.

(b) Key developments since Mr Douglas Rowe's letter of 18 September to FM/DFM:-

- **19 October** - Sir Reg Empey met representatives from the Petrol Retailers Association and agreed to write to Stephen Timms, First Secretary to Treasury;
- **20 October** - Sir Reg Empey wrote to Stephen Timms;
- **23 October** - Representatives from the Petrol Retailers Association met with Stephen Timms;
- **26 October** - OFM/DFM received a record of the meeting from Thomas Palmer, Chairman of the Petrol Retailers Association including his view that it was 'a very disappointing encounter';
- **6 November** - FM and DFM wrote to Chancellor seeking a meeting and responded to Mr Douglas Rowe informing of this.
- **November** - FM and DFM in their budget submission to the Chancellor stressed once more the need to reduce fuel duties.

(c) Current Fuel Duty Levels – NI compared with RoI

7. The current fuel excise duties for the UK (March 2000 Budget) are as follows:

- Unleaded petrol - 48.82 pence per litre
- Ultra low sulphur petrol - 47.82 pence per litre
- Ultra low sulphur diesel - 48.82 pence per litre
- (Virtually all diesel sold in the UK is ultra low sulphur diesel.)

8. These compare with fuel excise duties for the Republic of Ireland of (exchange rate of 1.25 IR£:£):

- Unleaded petrol - 21.9 pence per litre
- Diesel - 15.7 pence per litre

(d) Pre-Budget Report

9. In his Pre-Budget report the Chancellor proposed consultation on a package of measure for road transport:

   - a cash freeze on all road-fuel and other duties;
   - reduction of 2p per litre on the duty on Ultra-Low Sulphur Petrol
   - 3p per litre cut in duty on Ultra-Low Sulphur Diesel
   - extension of the 'small car ' threshold for vehicle excise duty from 1,200cc to 1,500cc;

- a 50% cut in, and reform of, vehicle excise duty for lorries
- abolishing vehicle excise duty on tractors;
- support for haulage industry including new driver training scheme and fund to help modernisation of vehicle fleet; and
- a user charge such as a 'vignette' for foreign hauliers using UK roads.

(NB all these measure except for the road-fuel and oil-duty freeze and the rebate of lorry VED this financial year, are subject to consultation)

(e) Decline in Fuel Deliveries to Northern Ireland

10. Official statistics (see Table 1) on deliveries of petroleum to Northern Ireland compiled by the Department of Trade and Industry show that road **fuel deliveries to Northern Ireland have fallen** over the last three years (1996/97 to 1999/00) as follows:

- Petrol - 37%
- Diesel - 51%
- Total - 43%

11. The **rate of decline is increasing** with almost half (47%) of the three year fall in the most recent year (year ending March 2000). The latest figures (April to July) show a continuing decline.

12. Over the last three years petrol/diesel deliveries to GB have remained largely unchanged at 36 million tonnes per annum.

(f) Increase in Licensed Vehicle

13. Over the three years 1996 to 1999 **the number of licensed vehicles in Northern Ireland grew** by 13%. This compares with an increase of 9% in the previous 3 years (see Table 2). This demonstrates that the decline in fuel deliveries direct to Northern Ireland in recent years is not due to declining demand for vehicles.

(g) The extent of smuggling

14. The extent of the fall over the last three years in officially recorded road fuel deliveries to Northern Ireland suggests a significant increase in fuel imports from the Republic of Ireland over this period. The figures above suggest that **40% to 50% of the fuel consumed in Northern Ireland is now supplied from the Republic**. Figures from the Legitimate Oil Pressure Group indicate that petroleum deliveries to the RoI grew by 24% in the period 1996-99 and that Northern Ireland's share of deliveries to the island of Ireland fell from just over a quarter in 1996 to less than a sixth in 1999.

15. While this may in part reflect the very high rates of growth in the RoI over this period it also supports the claim that currently imports from the RoI account for a

very large proportion of Northern Ireland petroleum consumption. **This can come from two sources – legitimate purchases by visitors/ shoppers to the Republic or smuggling.** There is no hard information on the extent of the latter. The view of the various petrol lobbyists is that smuggling is now being carried out on a wide scale and has begun to permeate the local petrol retail sector.

(h) Impact on the Exchequer

16. **HMT is a significant loser** as a result of the decline in Northern Ireland sourced petrol sales. Losses are **estimated to be in the region of £300m per annum**. There may be further losses to the HMT arising from the loss of VAT receipts due to consumers, initially attracted by lower petrol prices, also shopping more widely in the Republic.

17. There is also some evidence of loss of Vehicle Excise Duty receipts due to hauliers re-registering in the Republic though the recent announcements/proposals in the pre-Budget Report may reverse this. This loss of tax receipts is equivalent to a significant cash injection into the Northern Ireland economy, which benefits some fuel consumers (individuals and businesses) as well as those who are making huge gains from smuggling/racketeering activities.

18. The authorities in the RoI conversely gain from this around £130m per annum.

(i) Impact on Farmers

19. Farmers fuel cost are estimated to have increased by 25% in the last year.

20. The proposals in the Pre-Budget report will do little to reduce this. Many farmers are already exempt from paying vehicle excise duties on their tractors (tractors solely for farm use or for use within 5 miles radius of farms are exempt).

21. The cost of farm diesel, which is exempt from excise duty, will also not be affected by any wider freeze/reduction in fuel duties. For users of farm machinery it has been the significant increase in the cost of oil rather than excise duty levels over the last year or so which has been a cause for concern.

(j) Impact on Hauliers

22. Prior to the Chancellor's recent Pre-Budget Report, the Vehicle Excise Duties (VED) facing Northern Ireland hauliers were considerably in excess of those facing their RoI counterparts.The announcement of an immediate 50% cut in VED in the UK rate will considerably narrow the gap.

23. The proposed introduction of a user charge for foreign hauliers is likely to further reduce for Northern Ireland hauliers any VED disadvantage vis a vis their RoI competitors. (In the Pre- Budget Report Treasury indicated that following these

changes 'UK VED rates would be less than Sweden and broadly the same as in Germany, the Netherlands, **Ireland** and Belgium.' and ' for lorries that qualify for the reduced pollution discount the Government would expect typical UK VED rates to be less than in all these countries and comparable with France.')

24. While a considerable differential in fuel costs remains, Northern Ireland hauliers unlike their GB equivalents can access cheaper fuel fairly readily. This helps them to remain competitive vis a vis their RoI competitors.

(k) Impact on Petrol Retailers

25. The Petrol Retailers lobby has indicated that as a result of smuggling and consumers travelling to the RoI to buy petrol a large number of filling stations have closed in Northern Ireland over the last year or so. Figures provided by the Petrol Retailers Association suggest that over 70 (out of a total of 715) filling stations closed in the 14 months up to April 2000.

26. A report (May 2000) by the Legitimate Oil Pressure Group has indicated however that a number of 'closed' sites have been leased back from the owners by criminals and reopened for the sale of smuggled fuel. The same report also indicates that increasingly legitimate petrol retailers are accepting smuggled petrol (tempted by an extra £6000 profit per tanker load). The financial distress being suffered by retailers therefore needs to be qualified.

27. Mr Thomas Palmer in a letter (10 January 2001) to First and Deputy First Minister indicated that that in response to the collapse of the legitimate petrol retail sector in Northern Ireland that BP had decided to sell off their entire company network in Northern Ireland. Shell's retail presence in Northern Ireland is also, he claims, under review.

Table 1

Deliveries of Petroleum for use in NI
1992/93 to 1999/00
(Tonnes)

	Petrol		**Diesel**		**Total**	
	Tonnes	Index	Tonnes	Index	Tonnes	Index
1992/93	622438	100	348148	100	970586	100
1993/94	603566	96.97	368326	105.80	971892	100.14
1994/95	553144	88.87	373093	107.17	926237	95.43
1995/96	522523	83.95	356333	102.36	878856	90.55
1996/97	507082	81.47	370578	106.45	877660	90.43
1997/98	442488	71.09	324113	93.10	766601	78.99
1998/99	410335	65.93	265445	76.25	675780	69.63
1999/00	317736	51.05	180232	51.77	497968	51.31
						Source: DTI

Table 2

Motor Vehicles Currently Licensed in Northern Ireland
1992 – 1999

	Number	**Index**
1992	578312	100
1993	586325	101.39
1994	595951	103.05
1995	611562	105.75
1996	639286	110.55
1997	683569	118.20
1998	695360	120.24
1999	720645	124.62
		Source: DVLNI

Annex C

Meeting with the Chancellor – Introductory Speaking Notes

- Like to thank the Chancellor for meeting with us.
- Appreciate the solid environmental reasons for taxes on fuel.
- Recognise that high fuel prices are not a problem for Northern Ireland alone.
- Welcome the proposals in the Pre-Budget Report to reduce fuel and transport costs in general.
- Would like however to point out that Northern Ireland's **land border** with the RoI where petrol taxes are considerably lower than the UK **has led to significant problems** for Northern Ireland.
- It has led to competitiveness problems vis a vis the RoI for our road hauliers, farmers and businesses generally.
- For many this is on top of severe competitiveness problems arising from the high pound.
- One particular group which has been severely affected has been the petrol retailers. Legitimate petrol sales in Northern Ireland have fallen by over 40% in the last three years and the rate of decline is accelerating. Many petrol stations have closed particularly in border areas.
- Losses to the Treasury in excise duty are estimated to be running at over £300m per annum.
- This decline in petrol sales is not only due to consumers travelling over the border to buy petrol but to increased smuggling and illegal sales within Northern Ireland. Increasingly legitimate petrol retailers are being tempted to sell smuggled petrol (£6,000 profit per tanker

full!). There is evidence that major oil companies are ceasing to operate in Northern Ireland.

- This has become more than an economic problem involving a small number of petrol retailers. It has become a major law and order issue where involvement of paramilitaries in smuggling activity adds a further dimension.
- Like to discuss with Chancellor how this issue might be tackled.
- Also would like to use the meeting to raise several other issues which cause particular problems for Northern Ireland and where the effects can be perverse.

Annex D

MEETING WITH THE CHANCELLOR

FUEL ISSUES – LINE TO TAKE

It is recommended that the First Minister and Deputy First Minister use the meeting with the Chancellor to:

- Welcome the measures announced in the Chancellors Pre Budget Report but reiterate their continuing concerns at the high levels of fuel tax and transport costs in the UK and press him for further reductions.
- Remind the Chancellor of the serious consequences for Northern Ireland of the differential with the RoI with whom we have a land border. The adverse economic impacts on petrol retailers, on hauliers and businesses generally as well as the loss of Exchequer recepts should be mentioned. The focus should however be on the need to tackle the smuggling issue because of the law and order (including paramilitary) problems associated with it.
- Ask the Chancellor for an update on the Custom's recently introduced strategy to tackle smuggling and for the evidence (if any) of success.
- Introduce, if appropriate, any ideas emerging from the Northern Ireland Fuel Group on ways to reduce smuggling.
- To use the meeting to bring to the Chancellor's attention need for taxes generally to reflect the specific circumstances of Northern Ireland (eg the land border with the RoI) if perverse effects are to be avoided.

- Introduce the point that with a land border the proposed Aggregates Tax could also have adverse affects (separate briefing attached at Annex F);
- Also note the significant difference in Northern Ireland's energy costs and hence argue for a 10-year period for exemption from the Climate Change Levy (separate briefing attached at Annex E).

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