Economy, Energy and Tourism Committee

Future prospects for oil and gas in Scotland
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Economy, Energy and Tourism Committee

The remit of the Committee is to consider and report on the Scottish economy, enterprise, energy, tourism, renewables and other matters falling within the responsibility of the Cabinet Secretary for Finance, Constitution and Economy (apart from those covered by the remit of the Infrastructure and Capital Investment Committee), and matters relating to cities.

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## Committee Membership

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Introduction

1. The Committee held two oral evidence sessions, on 25 November and 2 December 2015, on the future prospects for oil and gas in Scotland. We wanted to consider the industry’s response to the significant and sustained fall in the price of crude oil since September 2014, and the consequences for jobs and the wider economy.

2. We heard evidence from trade union representatives about the impact on jobs, contractual terms and conditions and health and safety issues. These were among the issues we raised with Oil and Gas UK (O&GUK), the representative organisation for the UK Offshore Oil and Gas Industry, and the recently established regulator, the Oil and Gas Authority (OGA).

3. We were also keen to understand better how lower oil prices have impacted on the economy of Aberdeen and Aberdeenshire as well as the wider Scottish and UK economies. Aberdeen and Grampian Chamber of Commerce (AGCC) provided this perspective.
Executive Summary

4. This report examines the future prospects for the oil and gas sector in Scotland at a very challenging time for the industry brought about by a significant and sustained fall in the price of crude oil. We wanted to assess the impact on jobs, both offshore and onshore, and the implications for the economy of north east Scotland in particular. We also wanted to assess how some of the key players in the sector are responding to the current situation.

5. Our report is a snapshot in time. We recognise that there are a range of scenarios that might play out over the coming years. No one can predict with any certainty what the oil price will be 12 months from now let alone further into the future.

6. We believe that it is vital for the Scottish economy that Governments, the industry and the trade unions continue to work ever more closely together in order to ensure that the objective of maximising economic recovery of oil and gas from the UK Continental Shelf (UKCS) is fulfilled prior to the inevitable decommissioning phase of its life.¹

7. Our findings are presented in this short report which we have shared with the Scottish Government, Oil & Gas UK, the Oil and Gas Authority, the Health and Safety Executive, and the Maritime & Coastguard Agency for their response.

¹ Patrick Harvie dissented from this paragraph.
Current prospects

Oil price trends

8. International oil prices began falling in 2014, due in part to a slowdown in global demand as well as a continued high supply from OPEC and other producers. The price of Brent crude fell from over $100 per barrel in summer 2014 to $55 in December 2014. By the end of 2015 the price had fallen below $40 per barrel. Oil prices have fluctuated considerably since the 1970s. The graph below shows the trend.

Spot prices: Brent Crude Oil (US Dollars per Barrel) 1976-2015

Source: BP.com\(^1\) and U.S. Energy Information Administration\(^2\)

9. In a Staff Discussion Note, published in July 2015, the International Monetary Fund acknowledged that the oil price outlook is highly uncertain and subject to considerable short term volatility, but noted that futures markets imply an increase in Brent oil prices to some $75 per barrel in 2020.\(^3\)

10. Oil & Gas UK reported that between mid-2014 and the summer of 2015, the price of Brent futures for delivery in 2018 fell from $100 to $62 per barrel.\(^4\)

Job losses

11. The falling oil price has resulted in a spate of redundancies in the sector. Illustrative figures published by the Scottish Government in September 2015, sourced from media announcements, estimated that more than 6,000 ‘direct’ jobs had been announced as being “lost or at risk” since the downturn began.\(^5\) The actual figure is likely to be much higher, as these announcements did not include many self-employed contractors currently without work.
12. In its Economic Report 2015, published in September 2015, Oil & Gas UK estimated that employment supported by the sector in the UK, including direct, supply chain and ‘induced’ employment, had contracted by 15 per cent since the start of 2014 to 375,000 jobs. This equates to 65,000 jobs. The report stated—

“It is likely that capacity may have to be reduced still further in order for the business to weather the downturn.”

13. The STUC agreed that the O&GUK estimates were reasonable, but added that—

“... the situation has since deteriorated and that significant future job losses can be anticipated as current contracts expire and no new work is generated to absorb redundant workers.”

14. In its submission, the STUC stated that the falling oil price had led not only to significant job losses, but also “the imposition of major changes to collectively bargained terms and conditions and rising fears over the health and safety regime”. It also noted that the sector’s fortunes probably accounted for Scotland’s deteriorating economic and labour market performance relative to the UK through 2015, a view shared by the Fraser of Allander Institute in its recently published Economic Commentary.

15. In oral evidence, Tommy Campbell of UNITE told us—

“We reckon that approximately 6,000 jobs on the platforms and rigs themselves have gone and about 30,000 have gone in the support companies that back up the industry. Of course, rippling out from that, approximately another 30,000 jobs have gone in the hotel, catering and other sectors.”

16. James Bream, AGCC, reported that the number of jobs being posted with recruitment consultancies had halved since the same point in 2014.

17. Other anecdotal evidence suggests that in Aberdeen, hotel occupancy and room rates, pub and restaurant turnover, house sales and new car orders have all been impacted negatively by the downturn.

Energy Jobs Taskforce

18. In light of the downturn and the significant job losses in the sector, the Scottish Government established in early 2015 an Energy Jobs Taskforce. The Taskforce aims to—

- retain and grow the talent and skills in the industry;
- identify and implement support to people who are facing redundancy;
- enhance partnership and collaboration.
19. The Taskforce published an Action Plan which “aims to commit the North Sea Oil & Gas sector to work together to promote good practice, demonstrating and embedding behaviours that can protect and sustain industry jobs, and bringing to life the shared principles and values that are necessary”.  

20. In its most recent Progress Report, published in September 2015, the Taskforce recommended that “priority should be given to ensuring sustained support for those facing redundancy in the months ahead”. The report concluded—

“To summarise, the industry is on an improving trajectory that will focus on efficiency, value and collaboration underpinned by positive behaviours. Through strong leadership it will continue to build on the momentum already created and develop, promote and embed good practice regardless of the oil price.”

21. We support the aims and objectives of the Energy Jobs Taskforce which brings together industry, public sector and trade union representatives. We encourage it to continue to deliver its agreed action plan whilst ensuring that safety remains paramount.

**Short-term prospects**

22. Looking ahead, James Bream expressed the view that in the next year there would be “a slowing of the percentage rate fall in redundancies compared with the past year”, but “we are not at the bottom in terms of the reduction in employment—that is for sure.” Mike Tholen, O&GUK, added—

“Inevitably, there will be further job losses, not least because the outlook for the oil price remains much poorer than anticipated, even in spring this year.”

23. Deirdre Michie, O&GUK Chief Executive, told us—

“We are going through extremely challenging times as an industry and we expect those challenging times to continue. The situation is not likely to change much in 2016. However, as an industry, we are focused on and committed to continuing to ensure that we have a sustainable industry that can come through these difficult times and continue to provide economic value to Scotland and the UK.”

24. Andy Samuel, Chief Executive of the Oil and Gas Authority, talked about different future scenarios for the sector: some “good”, others “very difficult”—

“As a regulator, our job is to look to the future with different lenses and ensure that, regardless of things that we cannot control, such as the global price of oil, we are doing everything that we can to support maximising
economic recovery and, with that, investment. Jobs follow on from that. At the moment, I am more concerned than I am optimistic.  

<table>
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<th>25. We recognise the very challenging situation facing the oil and gas sector in Scotland brought about by the significant and sustained fall in the price of crude oil. Short term prospects, particularly for offshore workers, appear to be very difficult. However, we believe that with appropriate support from Governments, and enhanced collaboration, driven by the Oil and Gas Authority, a sustainable industry can emerge from this downturn.</th>
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<td>26. We also recognise the challenge in assessing the wider impact on the Scottish economy and suggest that the Scottish Government and its enterprise agencies consider whether more work requires to be done to establish the extent of this.</td>
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Health and Safety

Health and safety reporting

27. In light of concerns raised with us by the trade unions about an apparent reduction in health and safety incident reporting, we explored the reasons for what could be a worrying trend.

28. STUC had highlighted evidence from offshore unions that fear of redundancy was “critically undermining offshore health and safety as workers become reluctant to report actual and potential safety breaches”. It also reported serious concerns over helicopter safety.\textsuperscript{19}

29. In oral evidence, Stephen Boyd reflected on recent discussions with senior industry leaders—

\begin{quote}
I do not doubt any of their good faith when it comes to supporting an excellent health and safety regime in the North Sea, but the problem is that entering a rapid cost-cutting phase can introduce bad incentives along the chain of employment, particularly at the lower and middle management and the employee sides. There is no longer the incentive that should be there for employees to report every health and safety infraction, because of a concern that doing so would tag them for future redundancies.
\end{quote}

30. We asked the trade unions whether there was a system of anonymised reporting. Jake Molloy, RMT, replied—

\begin{quote}
There is a health and safety hotline but it is rarely, if ever, used, because of the regulator’s inability to make unannounced visits. The lead-in and investigation time would invariably identify the individual who is reporting. Therefore, in effect, the phones on my and Tommy Campbell’s desks are the hotline, and we deal with reporting that way.\textsuperscript{20}
\end{quote}

31. Responding to these concerns, Deirdre Michie said that O&GUK was aware of the unions’ concern. She said that the industry wanted to encourage people to be confident that they can report issues where they see them—

\begin{quote}
If there are concerns about the HSE whistleblowing line, which is the last defence, we need to address that. We should look at that so that people can feel confident that they can use the line and that their concerns will be listened to.\textsuperscript{21}
\end{quote}

32. The Health and Safety Executive rather than the OGA is responsible for health and safety regulation. A Memorandum of Understanding between the two organisations was signed in May 2015.\textsuperscript{22} Sir Patrick Brown explained that HSE
had “investigatory powers and enforcement abilities” and expressed the view that OGA should not get in the way of its work. However, he confirmed—

“... if we see things that it has not seen, of course we will let it know. However, it must be up to the executive to take the enforcement steps.”

33. Andy Samuel, OGA Chief Executive went further—

“If specific concerns are relayed to us, we will of course not just report them but make sure that they are followed up. That is a basic with safety—you do not just see it; you have to own it. My team will follow up on any matters.”

34. We welcome the commitment from Oil and Gas UK that it will address concerns raised about the operation of the Health and Safety Executive whistleblowing line. We ask to be provided with an update on this commitment by the end of February 2016. As part of this update, we ask for an affirmation on behalf of employers that workers can have confidence that reporting incidents will not have an adverse effect on their employment.

35. We welcome the development of close working relations between the Oil and Gas Authority and the Health and Safety Executive. We endorse the commitment from the OGA to report all concerns about safety raised with its staff to the HSE. We recommend that this be made explicit in the Memorandum of Understanding between the two organisations at its first review in May 2016. We believe that both the OGA and the HSE should recognise the importance of communicating their respective responsibilities to workers, and acknowledge the role of trade unions and elected safety representatives in reporting safety issues.

Maritime workforce issues

36. In its written submission, the STUC highlighted what it described as an increasing exclusion of UK seafarers from the North Sea due to “employers using gaps in employment legislation to employ non-UK seafarers below the UK minimum wage”. The STUC stressed that these practices were not evident in other North Sea jurisdictions similarly affected by the falling global oil price.

37. Asked whether the health and safety of seafarers in the oil and gas sector was being compromised by the use of flag-of-convenience vessels, Jake Molloy, RMT, replied—

“There is no doubt about it. I have done International Transport Workers Federation inspections on some vessels that have been flying the flag of convenience, and I know that the Filipino and Indonesian workers look upon us as the police arriving to save them from purgatory. The conditions...”
on some of those ships are appalling. What worries me most about that is that the industry has invested millions in developing competence to a standard that delivers safe operations, and that is being dumped. Less competent, less able and less willing workers are being exploited in order to exploit our natural resources.\(^{26}\)

38. Mr Molloy explained that in the North Sea, British seafarers had taken a 25 per cent wage cut resulting in a salary of only £23,000 a year and now worked six days on, six days off “to try to save their jobs and compete”.\(^{27}\) In relation to possible legislative action which could be taken to address this, he told us—

> The only way that I see the demise of the British and EU seafarer being averted is through an EU caveat and an EU cabotage structure that restricts employment on vessels that service the exploitation of our natural resources to EU and UK seafarers who are paid at minimum wage—I would even accept that as a starting point.\(^{28}\)

39. We recognise that the Maritime & Coastguard Agency (MCA), an executive agency, sponsored by the UK Department for Transport, is responsible for the safety of everybody in a vessel in UK waters. It is also responsible for the production of legislation and guidance on maritime matters, and providing certification to seafarers.\(^{29}\)

40. We invite the Maritime & Coastguard Agency to respond to the concerns raised with the Committee by trade union representatives in respect of health and safety on flag of convenience vessels and the remuneration of non-UK seafarers below the UK minimum wage. We ask also for an update on recent UK Government engagement at an EU level to protect and enhance the working conditions of UK seafarers.
Maximising economic recovery versus decommissioning

41. We heard evidence about the increased likelihood of ageing infrastructure in the oldest UKCS fields being decommissioned earlier than envisaged because of the decline in the oil price.

42. In its most recent Economic Report, O&GUK discussed how the industry might respond to the challenge presented by the falling oil price—

> A continued low oil price will inevitably cause companies to reflect on the future viability of their assets. Retaining infrastructure and delaying decommissioning will be key to prolonging production from existing fields and promoting future developments.\(^{30}\)

Maximising economic recovery

The Wood Review

43. Sir Ian Wood’s review (“the Wood Review”) of UKCS oil and gas recovery, looking specifically at how economic recovery could be maximised, published its final report on 24 February 2014.\(^{31}\) It called for Government and industry to develop and commit to a new strategy for Maximising Economic Recovery (MER) from the UKCS. Perhaps its most radical recommendation was to form a new ‘arm’s length body’, effectively a new regulator, which would be ‘charged with effective stewardship and regulation of UKCS hydrocarbon recovery and maximising collaboration across the industry’. The Oil and Gas Authority was established in response to this recommendation.

Enhanced collaboration to drive down costs

44. The Wood Review envisaged that a new, stronger regulator with broader skills and capabilities would be able to enhance significantly the level of industry co-ordination and collaboration. Sir Ian considered that this would help to maximise economic recovery of UKCS oil and gas. It would also serve to increase efficiency and reduce costs.

45. Asked by how much costs need to reduce to meet a break-even price to sustain production, Mike Tholen, O&GUK, told us that there was no “one-size-fits-all” answer—

> In the early years of production, the break-even price for a new field was much lower than we see in today’s market. Most fields in the North Sea are in their middle age or are even more mature than that, so we are having to manage a much greater balance of cost and relatively low production by those facilities.\(^{32}\)
46. Andy Samuel agreed with this view—

> The main reason why the UKCS is higher cost … is that we now have 300 fields producing a third of what they used to produce, as compared with, say, Norway, which has a third fewer fields producing quite a bit more. The mathematics mean that the cost per barrel goes up.\(^{33}\)

**Diversification and internationalisation**

47. Stephen Boyd, STUC, talked about the importance of Scottish Government support for both collaboration and diversification—

> Scottish Enterprise is playing an important role in the north-east, particularly at the moment through Lena Wilson’s chairing of the energy jobs task force but also in having tried to drive that collaboration in the past. The Scottish Government needs to resource that activity and must look closely at the real opportunities for diversification and what Government investment is required to realise those opportunities.\(^{34}\)

48. Deirdre Michie also referred to the business opportunities arising from diversification and exports—

> We have a very strong supply chain that is rooted in the UK but has a strong export business. As we go forward, we need to think about how we support those companies and ensure that they anchor themselves here but are looking to diversify and improve their export opportunities.\(^{35}\)

49. The most recent AGCC oil and gas survey, published in November 2015, noted that survey respondents had, typically, been more optimistic about their international activities in recent surveys. The current outlook was, however, less positive—

> While this continues in this survey, we see negative net balances on both current optimism levels in international markets, and optimism over the next 12 months. This is the first time that the survey has recorded both “international” measures for optimism as negative for two consecutive surveys.\(^{36}\)

** Decommissioning**

50. In its written submission, the STUC had stated that the approach to maximising economic recovery must also seek to—

> … maximise wider economic and employment benefits through, for example, developing a proactive and effective approach to decommissioning.\(^{37}\)
51. Stephen Boyd emphasised that decommissioning should be seen as a future opportunity as it could provide “a route to diversification and saving jobs and an opportunity for Scotland to develop expertise that can be exported around the world”. He went on to say—

> Even if we took climate change right out of the equation and focused on the change in the economics of the oil industry that I discussed earlier, you would still have to shift towards looking at the transition happening much earlier than was previously anticipated.

and—

> All those things [projections for fossil fuel consumption] taken together with the change in economics suggest that we have to be planning for the North Sea to have a shorter lifespan than previously thought.

52. Mike Tholen told us—

> We are in a period of painful readjustment and some fields will inevitably be decommissioned because very low oil prices mean that they have reached the end of their productive life more quickly, but there is still a future out there for our business.

53. However, when asked about opportunities which would arise from future decommissioning, Deirdre Michie emphasised that O&GUK did not want to see an acceleration towards this—

> We need to maximise economic recovery, which is what the Wood review was focused on and what Andy Samuel and his team [OGA] want to ensure that we drive for. We have to push out the economic recovery of the basin for as long as we can. We know that we have to move to decommissioning at some point, but we need to ensure that we do that when the time is right and that we do it safely and efficiently. It can never replace the industry that we have, because it will not support security of supply or the same number of jobs. However, the UK can be a centre of excellence for decommissioning.

54. The Wood Review recommended the creation of a decommissioning strategy to “achieve the maximum economic extension of field life and to ensure key assets are not decommissioned prematurely to the detriment of production hubs and infrastructure”.

55. In its draft Corporate Plan, the OGA reported that it had recently conducted a detailed field by field analysis which estimates decommissioning costs for 2015 to 2050 at £47 billion. However, it also stated that a successful decommissioning strategy could deliver estimated overall savings of £16 billion.
56. Andy Samuel, OGA, told us that it had recently formed a single decommissioning senior board which would report to the MER UK forum. He suggested that decommissioning was a great opportunity for the service sector which could create “international competitive advantage” if done correctly. Mr Samuel urged transparency and co-operation between operators in order to phase work and reduce costs. To this end, he considered that the OGA had a role in “scanning the forward horizon”. He concluded—

“There is quite a lot that we can do. The strategy is being actively formulated right now.”

57. We ask the Oil and Gas Authority to provide the Committee with its decommissioning strategy, plan and 10 year roadmap once finalised in the first quarter of 2016.

58. We encourage the Oil and Gas Authority to work with the industry and public sector partners, such as Scottish Development International, actively to identify international decommissioning opportunities for Scottish contractors.
Conclusion

59. The oil and gas sector is facing extremely challenging times at present with the significant and sustained fall in the price of crude oil since September 2014. The impact on jobs and wider consequences for the economies of the north east, Scotland and the UK is significant.

60. Our report is a snapshot in time. We recognise that there are a range of scenarios that might play out over the coming years. No one can predict with any certainty what the oil price will be 12 months from now let alone further into the future.

61. We believe that it is vital for the Scottish economy that Governments, the industry and the trade unions continue to work ever more closely together in order to ensure that the objective of maximising economic recovery of oil and gas from the UKCS is fulfilled prior to the inevitable decommissioning phase of its life.

62. We invite the Scottish Government, the Oil and Gas Authority, Oil & Gas UK, the Health and Safety Executive and the Maritime and Coastguard Agency to respond to the issues raised in this report.

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2 U.S. Energy Information Administration. (2015) *Spot Prices (Crude Oil in Dollars per Barrel, Products in Dollars per Gallon).*
3 International Monetary Fund. (2015) *Global Implications of Lower Oil Prices. IMF Staff Discussion Note SDN/15/15.*
7 STUC. Written submission.
8 STUC. Written submission.
19 STUC. Written submission.
22 Health and Safety Executive and Oil and Gas Authority. (2015) *Memorandum of Understanding between the Health and Safety Executive and the Oil and Gas Authority Concerning Effective Cooperation and Communication Arrangements.*
Annexe A

Extracts from the minutes of the Economy, Energy and Tourism Committee and associated written evidence

30th meeting, 2015 (Session 4), Wednesday 25 November 2015
1. Decision on taking business in private: The Committee agreed to take item 4 in private. The Committee also agreed to review evidence heard at future meetings, in connection with future prospects for oil and gas in Scotland, in private.
3. Future prospects for oil and gas in Scotland: The Committee took evidence from—
   Stephen Boyd, Assistant Secretary, Scottish Trades Union Congress;
   Jake Molloy, Regional Organiser, RMT;
   Tommy Campbell, Industrial Organiser, UNITE.
4. Future prospects for oil and gas in Scotland (in private): The Committee reviewed the evidence heard at the meeting.

Written evidence

STUC

31st meeting, 2015 (Session 4), Wednesday 2 December 2015
3. Future prospects for oil and gas in Scotland: The Committee took evidence from—
   Deirdre Michie, Chief Executive, and Mike Tholen, Economics Director, Oil & Gas UK;
   James Bream, Research and Policy Director, Aberdeen and Grampian Chamber of Commerce;
   Andy Samuel, Chief Executive, and Sir Patrick Brown, Chair, Oil and Gas Authority.
4. Future prospects for oil and gas in Scotland (in private): The Committee reviewed the evidence heard at the meeting.

32nd meeting, 2015 (Session 4), Wednesday 9 December 2015
2. Decision on taking business in private: The Committee agreed to consider a draft report on future prospects for oil and gas in Scotland in private at future meetings.
2. Future prospects for oil and gas in Scotland: The Committee considered a draft report. Various changes were agreed to, and the report was agreed for publication.

* * * * * * * *

Note of divisions in private: Patrick Harvie proposed that at paragraph 21 the Committee recommend that the Energy Jobs Taskforce be given an additional explicit aim of supporting the transition to non-fossil fuel industries including decommissioning and renewables. The proposal was disagreed to by division: For 1 (Patrick Harvie), Against 8 (Chic Brodie, Murdo Fraser, Johann Lamont, Richard Lyle, Lewis Macdonald, Gordon MacDonald, Joan McAlpine, Dennis Robertson), Abstentions 0.

Patrick Harvie proposed that the final sentence of paragraph 25 be deleted and the following text inserted—

“However, we believe that with appropriate support from Governments, and enhanced collaboration, a transition towards more sustainable industries can emerge from this downturn.”

The proposal was disagreed to by division: For 1 (Patrick Harvie), Against 8 (Chic Brodie, Murdo Fraser, Johann Lamont, Richard Lyle, Lewis Macdonald, Gordon MacDonald, Joan McAlpine, Dennis Robertson), Abstentions 0.

Patrick Harvie proposed the insertion after paragraph 57 of the following text—

“We recognise the need to accelerate the shift toward decommissioning work, and are concerned that Scotland is already at risk of losing out on contracts for such work to other countries.”

The proposal was disagreed to by division: For 1 (Patrick Harvie), Against 8 (Chic Brodie, Murdo Fraser, Johann Lamont, Richard Lyle, Lewis Macdonald, Gordon MacDonald, Joan McAlpine, Dennis Robertson), Abstentions 0.

Patrick Harvie proposed that paragraph 61 be deleted and the following text inserted—

“We recognise that the employment opportunities relating to the UKCS will inevitably shift toward decommissioning, and that Scotland is in danger of missing this opportunity if the strategic priority remains maximising extraction. Given that global fossil fuel reserves already far exceed the limits of sustainable consumption, we consider that government policy must be urgently realigned to support the transition away from the current reliance on fossil fuels, and toward the sustainable jobs which can be generated in a post carbon economy.”

The proposal was disagreed to by division: For 1 (Patrick Harvie), Against 8 (Chic Brodie, Murdo Fraser, Johann Lamont, Richard Lyle, Lewis Macdonald, Gordon MacDonald, Joan McAlpine, Dennis Robertson), Abstentions 0.