

2. Setting our charges

2.1. Our charges - our aims

We charge to make sure we can cover our costs when exercising our regulatory functions.

Those functions consist of:

- services that we make available to all in the regulated community, which are accessed 'on demand'
- other activities we tailor in a planned way to ensure we deploy our resources effectively and efficiently to achieve the aims of the regulations

This means:

- We receive full cost recovery, to include administration, environmental planning and assessment, registration, monitoring, permitting and compliance assessment (plus associated corporate costs) with no cross-subsidy between regimes
- Our charges reflect our regulatory effort
- Cost recovery is stable from one year to the next, and charges are broadly predictable and don't create perverse behaviours
- Customers understand the basis for our charges and what level of charge and service they can expect from us
- We can demonstrate that we are cost-effective, and deliver ongoing efficiency gains for both us and our customers
- Our charging schemes reflect the requirements of HM Treasury's Managing Public Money guidance

2.2. Our current charging schemes

Environmental Permitting

The Environmental Permitting Regulations brought together several previous permitting systems into one so we already have a commonality in our approach to regulating these activities. There were also several relevant charging systems, however these were not reviewed at that time to fully reflect our new ways of working. For example, one of the existing charging systems (for discharges to water) has not changed significantly since its implementation in 1992.

The current use of the Operator Risk Assessment (OPRA), Charges for Discharges (CfD), Tier 2 charges and look-up tables has led to a complex set of calculations so that arriving at the correct application charge needs a degree of skill on an operator's part, or assistance from us in pre-application discussions.

For EPR activities particularly, we are aiming to implement simpler and more consistent charging arrangements.

Other charging schemes

For other activities not under the EPR (such as EU ETS, Navigation, Water abstraction, COMAH and WEEE) see section 2.5.

2.3. How we have approached the review of charges for EPR regimes

We looked through the permits under the various regulatory regimes in EPR (Waste, Installations, Water Discharges, Radioactive Substances Regulation, and Flood Risk Consents) to reflect on our different levels of regulatory effort.

The factors that can define our approach at a regulated facility are:

- the nature of the activity
- the scale of the activity
- the location of the activity in relation to the risk posed to the local environment (applications only)

We reviewed our permitting and compliance work, with the use of time recording and expert judgement, to assess our different levels of regulatory effort. We use a mix of different regulatory interventions to assess different applications, to ensure that permits are complied with and standards remain appropriate.

All permitted activities have been placed into categories based on our regulatory approach and effort to control the risks posed by the operation (e.g. balance of on-site versus off-site regulation) and therefore the different costs of regulation.

All told, our proposals now include some 250 permit categories (annual subsistence charges) and some 275 different application charges. Supplements may also apply. This compares to over 3,000 different subsistence and application charges levied under our existing charging systems.

We will charge either using fixed charges where costs are known up front and are payable at the point of application, or use a time and materials approach which allows us to use a pre-calculated hourly rate for work of variable lengths and invoiced accordingly.

New Application charges

Activities that we undertake each time we issue a particular permit are included in our baseline application charge. Additional assessments that may be needed will be charged as additional components. The range of additional components that could apply is listed in Section 2.1.12 of the Guidance to the EPR Charging Scheme. Examples include: sensitive locations assessment for sites designated under the Habitats Directive, or Fire Prevention Plans where the waste types and activities covered by the application would lead us to believe there is a risk of waste fires.

Levying additional supplementary charges for only those applications that involve more complex considerations also means that we can offer the most cost reflective 'baseline application charge' for the simpler applications, which can reduce barriers to entry and encourage growth.

We have tested this approach and have found it to be much simpler and faster to calculate than the previous OPRA based system.

The specific application baseline charges are detailed in the Application charges tables.

Supplementary application charges are described in section 2 of the Guidance to the EPR Charging Scheme.

New Subsistence charges

To ensure full subsistence cost recovery, we reviewed each category of permit in each sector to quantify the effort required for effective regulation. The breadth and diversity of activities requiring permits means that there is significant tailoring of our regulatory activity to different permitted activities.

In common with our application charges approach above, we considered both the work of our operator facing teams who deliver the most visible aspects of our regulation, and also that of the other teams who are contributors, within the Environment Agency and the Defra family.

The specific baseline charges are detailed in the Subsistence charges tables.

As with application charges we are proposing some fixed cost supplementary subsistence charges, to recover costs for more unusual or one-off events, including a 'first year charge' (See Section 4.6.2 of this document) and a charge for the review of a waste recovery plan (See Section 4.3.2 of this document). These too are described in the Guidance to the EPR Charging Scheme.

2.4. Supplementary time and materials charges

Our wholly predictable and planned regulatory activity can be funded through fixed annual subsistence and application charges as described above.

We also intend to use time and materials, at a defined hourly rate, or other supplementary fixed charges, where we incur unusual and less predictable costs dealing with specific customers. This approach will allow more targeted and timelier cost recovery for resource deployed over and above that planned and recovered via baseline charges.

This enables us to target the recovery of costs in-year from the responsible person for unusual activity and events that are not part of the usual planned regulatory activity at all sites. An example of this would be the follow-up work assessing reports or fresh proposals, related to 'improvement conditions' imposed in a permit variation. This work is independent of activity covered by our baseline charges and seeks only to recover additional costs we incur in year on a case by case basis.

The circumstances in which we'd apply fixed charges and time and material supplementary charges are specified in section 4. Further information is within the consultation and related guidance documents. In each circumstance the customer will have a clear indication of when supplementary charging will apply. In the case of time and material charging, this provision will only be used in specific, limited circumstances. We will notify operators when they are entering time and materials supplementary charging, and keep them informed of estimated costs of on-going supplementary work.

Consultation question

1. Do you agree with the proposals to charge fixed charges where we have greater certainty over costs and time and materials in other instances?

- Yes
- No
- Not applicable

If not, please explain why.

2.5. How we have approached the review of charges for other regimes and discretionary services

For other activities not under the EPR (such as EU ETS, Navigation, Water abstraction, COMAH and WEEE) we followed a similar approach to that above. We:

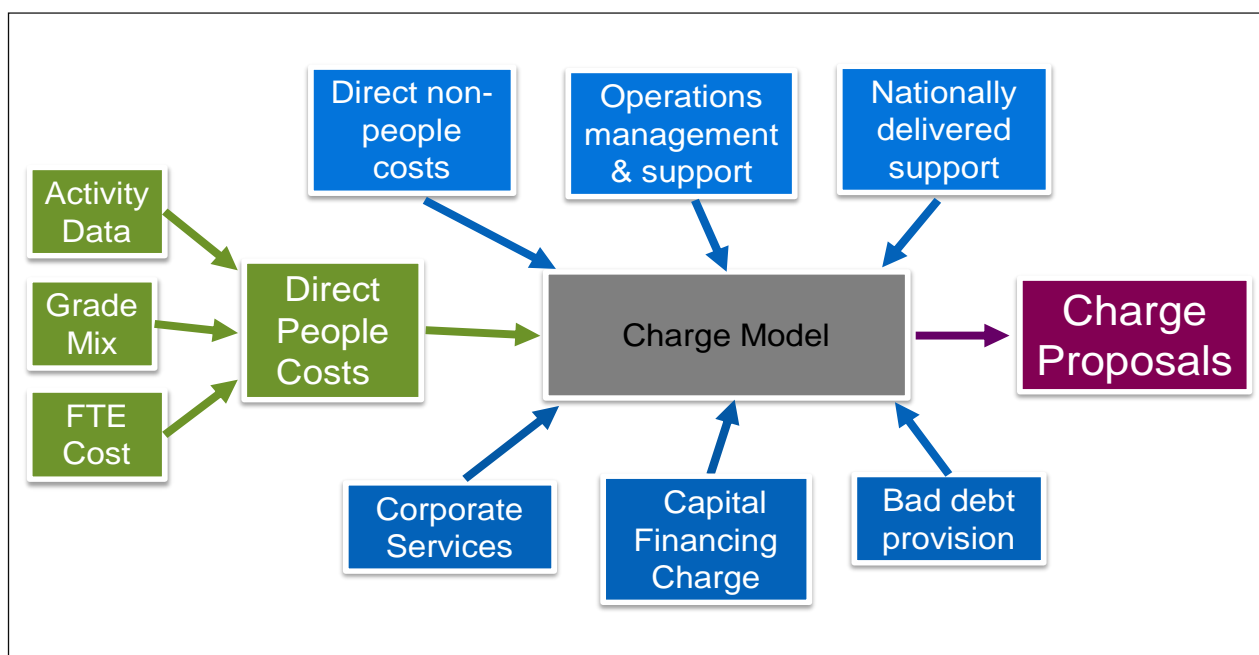
- assessed our current regulatory system or service and how much resource we need
- identified all the activities carried out to deliver our statutory duties, and the outputs produced by those activities
- explored any simplification opportunities available that could make our desired activity even more cost-beneficial
- developed charges for new services, where applicable

2.6. How have we modelled our charges

We are required to follow HM Treasury's Managing Public Money (MPM) and Classification of Receipts guidance when calculating the costs of our services and setting our charges. These guidance documents ensure that all government departments and public bodies collect and spend your charges correctly by setting out what we can, and cannot, charge for. HM Treasury scrutinise all our proposals against these rules.

We have modelled the costs required to regulate permits in a consistent manner across all our major regimes (with the exception of water abstraction). Modelling for our remaining regimes will follow.

The diagram below shows the types of cost that are included in our modelled charge proposals.



Direct delivery costs

Direct delivery costs can be delivered locally, for example by area or water catchment experts, or nationally by specialist teams such as our National Permitting Service.

We have modelled our revised charges based on our assessment of the time we need to spend on our regulatory activities for each permit category in each regime, and the average grade mix of the teams that will carry out the tasks. Our baseline activities have been assessed by considering operators that are compliant with their permit conditions. The proposed charges are then calculated based on our average hourly cost of the staff undertaking these activities (including National Insurance and pension costs), and other costs identified in MPM guidance as recoverable, such as travel. We use data on actual current costs to inform (but not determine) the future level of these costs in our models. These costs are attributable directly to the customer, either as a cost for a particular permit category or as an hourly rate.

Indirect costs – support services to enable direct delivery of work

These are services provided across all our chargeable and non-chargeable work, whose costs are recoverable under MPM guidance. Without support services, a regulatory regime and charging scheme could not operate.

During 2010 to 2017, we have delivered two major reorganisations to reduce expenditure and increase efficiency, centralising services where appropriate. As a result some of our direct delivery activities now operate from within our indirect functions, such as guidance development for delivery staff.

All our staff, whether operational staff who do the "front line" work or support staff need such services as:

- training
- technical support and guidance
- legal advice to ensure they operate within the law
- HR policies and advice from HR business partners for line managers
- transactional finance staff to raise invoices, deal with payment queries and chase payments
- financial planning, performance monitoring, statutory accounting and auditing
- fully functioning and maintained buildings
- IT systems and communication devices to do their work, store work securely and an IT helpdesk and other resources to resolve technical problems

Some of these services are now being delivered by the new Defra Corporate Service as part of the Defra Transformation Programme. Future efficiency savings due to be delivered by this new consolidated service have been included in the charge proposals. All of Defra's delivery bodies are required to recover their relevant share of the Defra Corporate Service costs from their charge payers.

The services that remain delivered by Environment Agency staff exist to support the whole of our business, both direct and indirect functions. They are not always easily allocated directly back to specific sources of income but nevertheless we are required under MPM guidance to ensure that all charge payers make a fair contribution to indirect costs. In order to do this therefore we apportion indirect costs across all funding streams in proportion to their annual revenue costs.

Fixed costs

We have some fixed costs within the Environment Agency that are not variable to changes in staff activity levels, or volume of work increasing or decreasing. They can be contracts that have to be paid regardless of our activity levels. These are included in our modelling to ensure we recover the total of the fixed cost, including any contractual increases which are often linked to the Consumer Prices Index (CPI).

Financing costs

We are required to include the depreciation and cost of capital related to the fixed assets used by each regulatory regime. These assets include specific assets used exclusively by the regimes, and a proportion of corporate assets (such as IT systems and buildings) used by many regimes. We calculate the annual depreciation charge by using the net book value and remaining asset life. The cost of capital is calculated as 3.5% of the average net book value throughout the year.

Bad debt

We are required to include a provision for bad debts in our charges, to cover unpaid charges that we cannot recover through our normal debt recovery process. An example of this would be where a company has gone into liquidation. The level of bad debt varies by charging scheme due to different levels of credit risk.

Cost pressures

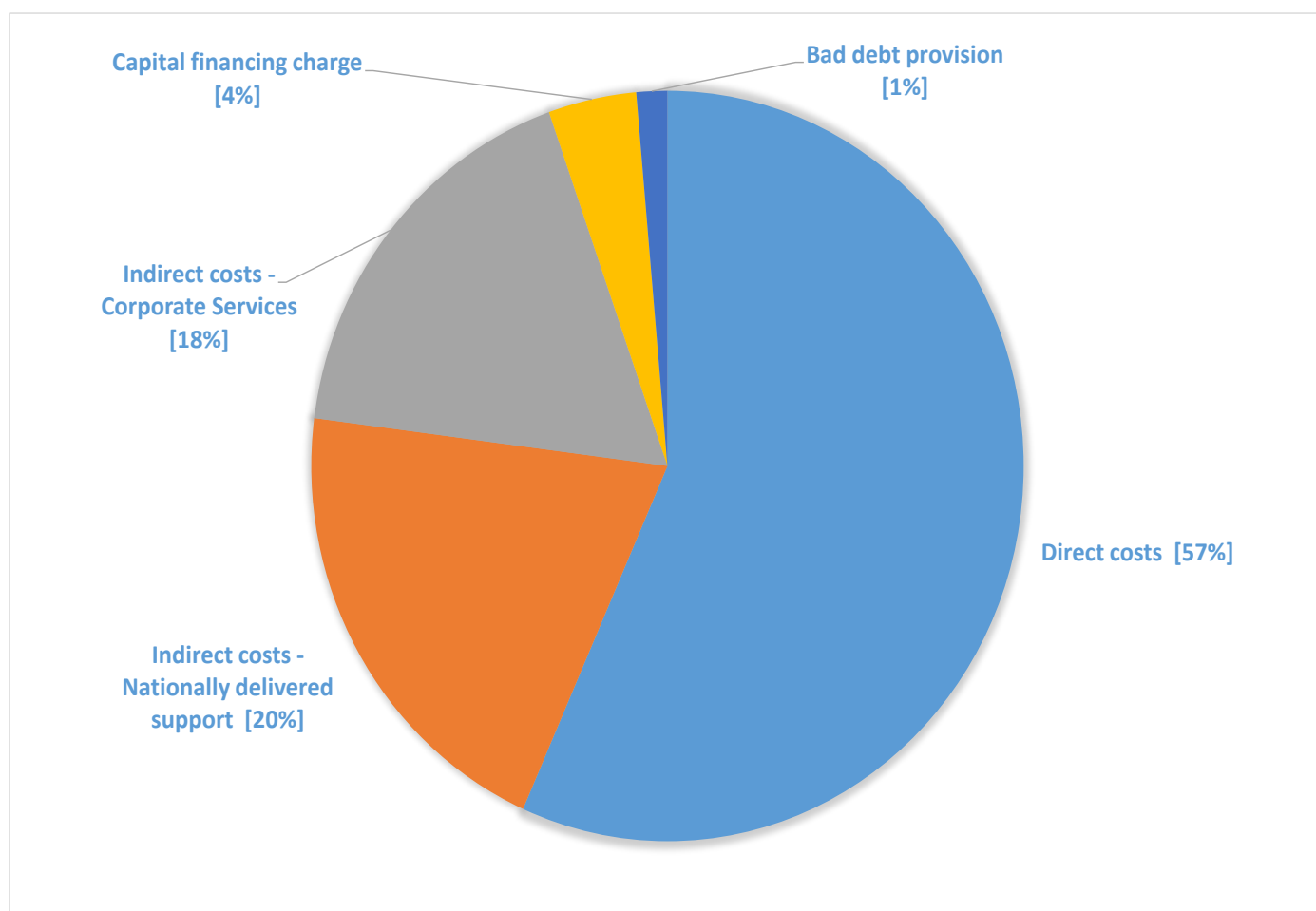
We have built inflation into our proposals at the current government CPI projections, with the exception of pay inflation which has been capped at 1% per annum. Staff costs form the majority of

our direct costs. We have also overlaid efficiency savings where we have change programmes already planned for (see Efficiency Savings section below).

We are proposing to hold our charges unchanged through the 5 year period, with inflation expected to be offset by efficiency savings. Should our assumptions for inflation and efficiency programmes prove to be materially out of line with actual results, the Environment Agency would bear a significant financial impact. We therefore propose to review our charges mid-way through the 5 year period to ensure we are not materially over-recovering or under-recovering our costs.

A typical breakdown of our costs for each regulatory regime is illustrated in the following pie chart:

Distribution of charge income



2.7. Efficiency savings

2.7.1. Plans for future efficiencies

We have plans for future efficiency measures, which have been reflected in our charge proposals.

Examples include:

- savings from the Corporate Services changes delivered through Defra's Transformation Programme

- undertaking a strategic review of environmental monitoring and implementing Defra Group's Digital transformation
- working with Defra Digital Services to trial a new system for the Waste Industry to make application and management of permits more efficient
- various industries, led by landfill, will be able to submit their monitoring compliance data digitally using the Data Returns Service - this will simplify our customer interactions and eliminate technical and process duplication.

2.8. Transition from existing scheme to proposed scheme

We propose to implement the proposed charges from 1 April 2018. The intent is that from that date the new charging provisions will apply to our future regulatory actions. However, 'fully paid for' regulatory activities that are in progress having been commenced before that date, will be completed under the remit of the existing charging scheme.

For example, this means that applications received before 1 April 2018 will pay application charges due under the existing scheme. There may be subsequent supplementary charges due where advertising is necessary, or where applications are subsequently amended by the applicant. These supplements would have been due under the existing scheme and will continue to be due under the proposed scheme at the same charge. No new supplements due under the new scheme will apply to such applications, so we would not, for example levy supplementary charges relating to extended consultation for sites of high public interest.

Annual subsistence charges for existing permits will be levied at the proposed rates set out in this consultation for 2018/19. These baseline charges do not cover any unusual or exceptional regulatory effort that may be required. Hence, any additional work that we undertake after 1 April (for example in responding to exceptional pollution events; in assessing submissions made to us in response to permit conditions, etc) will incur supplementary charges as set out in this consultation.

We have proposed a supplementary charge to provide additional early engagement with a new operator. We propose to have a first year charge to cover the costs of an additional site visit and advice, when these sites first commence operations. This would apply to activities that commence after 1 April 2018.

Consultation Question

2. Please tell us if you have any comments about the proposed transitional arrangements outlined in section 2.8