HM Treasury

Oil and Gas Fiscal Review

Outcome and summary of responses

November 2023

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Chapter 1
Introduction

1.1 In the 2022 Autumn Statement, the Chancellor announced a review into the long-term fiscal regime for oil and gas to ensure the regime delivers predictability and certainty, supporting investment, jobs and the country's energy security.

1.2 The government published the Terms of Reference for the review in June 2023. These set out the intention to consider whether and how the fiscal regime can support investment in the UK consistent with the UK's energy security and net zero ambitions by:

- Supporting UK energy security and helping to meet domestic energy demand, as we transition to net zero, through incentivising activity that maximises economic recovery of the UK's oil and gas resources in the medium term;
- Promoting the pathway to a net-zero basin by 2050 through supporting the decarbonisation of upstream oil and gas activities as set out in the North Sea Transition Deal (NSTD);
- Prioritising long-term energy security, and responding to the diversification of activity in the basin in a way that minimises barriers to investment in greener technologies;
- Being made more efficient and predictable, including in its response to any future price shocks and persistent price volatility as well as through further simplification;
- Delivering a fair return on the nation's resources to support the public finances and fund vital services.

1.3 The government published a Call for Evidence (CfE) which ran from 31 July 2023 to 11 September 2023, seeking views on the evolving context of oil and gas production and how the design of the long-term fiscal regime has an impact on the activity of the sector. During this period, HM Treasury also held a series of engagement in London and Aberdeen, including a launch event, five thematic roundtables and around thirty one-to-one meetings with relevant stakeholders. The review has been led by HM Treasury, working closely with HM Revenue & Customs (HMRC), the Department for Energy Security & Net Zero (DESNZ) and the North Sea Transition Authority (NSTA).

1.4 The focus of the review is on the long-term future for the regime rather than short-term changes to the current fiscal regime. Therefore, changes to the Energy Profits Levy (EPL) were not considered as part of the call for evidence.

1.5 While demand for oil and gas will decline, they will retain a crucial role as critical fuels that play an important part in ensuring secure energy supplies. The government's Powering Up Britain: Energy Security and Net Zero Growth Plans formed an important foundation for the review's objectives. As oil and gas consumption was considered in these documents, it was not reconsidered as part of this review.

1.6 Mainstream elements of the UK tax system as they apply to the industry and its supply chain, including income tax, National Insurance contributions, VAT and mainstream Corporation Tax are also out of scope of the review - changes to these are considered in the context of the wider UK tax system.

1.7 The following chapters set out the final outcomes of the Oil and Gas Fiscal Review and a summary of responses from the CfE.

Chapter 2
Fiscal Review Outcomes

2.1 The government is grateful to all respondents who took the time to engage with the Oil and Gas Fiscal Review, which has informed continued policy development. Officials also directly engaged with representatives from industry trade bodies, businesses operating in the sector, environmental groups and the renewable energy sector. HM Treasury worked closely with HMRC, DESNZ and the North Sea Transition Authority (NSTA) to ensure a wide range of evidence across government informed the outcome of the review.

2.2 Oil and gas taxes make a significant contribution to the UK's public finances, helping the government to support those most in need. To date over £400 billion in direct taxes (in 2022/23 prices) have been generated from domestic oil and gas production. According to Offshore Energies UK, in 2021 around 200,000 direct, indirect or induced jobs were supported by the sector[1].

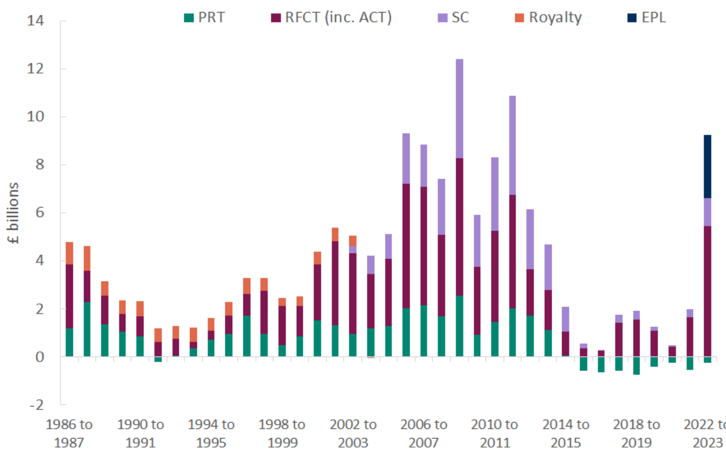

Figure 1 - Contributions to public finances from oil and gas production

2.3 Oil and gas also currently contribute around three quarters of the UK's energy demand [2].While the government is scaling up homegrown clean energy sources such as offshore wind and nuclear, the UK still relies on oil and gas and this will continue to be the case over the coming decades. As the government takes forward a pragmatic, proportionate and realistic response to the path to net zero, a key part

[1] OEUK Workforce Insight 2022, https://oeuk.org.uk/wp-content/uploads/2022/11/OEUK-Workforce-Insight-2022.pdf

[2] DESNZ, Supply and Use of Fuels, Energy Trends Table 1.3 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1147082/ET_1.3_MAR_23.xlsx

of this will be maintaining our domestic oil and gas industry which underpins our energy security and boosts the UK economy. Domestic production also means the government can influence how cleanly it is produced.

2.4 This chapter sets out the outcomes of the Oil and Gas Fiscal Review, taking into consideration CfE responses. These look to promote oil and gas investment, recognising the positive impacts of the domestic oil and gas sector in the wider economy and its important role in underpinning energy security of supply. The government recognises that certainty and predictability are critical to maintaining investment across the sector. The outcome of the review therefore seeks to entrench a principle of predictability and certainty in the design of the long-term tax regime.

2.5 The government recognises that many stakeholders noted views about the Energy Profits Levy (EPL), a new, temporary, levy on ring fence profits of oil and gas companies, in their responses to the fiscal review. As part of Autumn Statement, the government is also setting out next steps on the Energy Security Investment Mechanism (ESIM), the EPL's price floor.

2.6 Oil and gas investment is also enabled by a predictable regulatory regime through oil and gas licensing. The NSTA recently announced 27 licences offered in the first batch of the 33rd Oil and Gas Licensing Round. These are the first to be awarded from 115 applications – the highest participation since 2016/17 29th Licensing Round. The introduction of the Offshore Petroleum Licensing Bill will make the UK more energy independent by increasing investor and industry confidence with regular annual oil and gas licensing. The Bill's tests will ensure that future licensing supports the transition to net zero.

Supporting investment through predictability and certainty

2.7 Oil and gas investment is important given the sector makes a significant contribution to the economy, supports jobs, funds public services and underpins our energy security. The review was announced to consider the long-term future of the oil and gas fiscal regime, beyond 2028 and has provided an opportunity to consider how the investment context will continue to evolve as the basin matures and market conditions change.

2.8 The government has heard loud and clear that in the fiscal regime certainty and predictability are the most important influence on investment, noting feedback that investment incentives in the permanent regime support investment well and calls from some stakeholders to reduce investment support in future. The government also recognises strong views about the EPL and that uncertainty about what happens after the EPL ends can make investment decisions harder to make.

2.9 **To support predictability and certainty, the fiscal review re-confirms that the EPL will end in March 2028, or earlier if the ESIM is triggered.**

2.10 By their nature oil and gas price shocks happen infrequently and are unexpected. Whilst the permanent tax regime works effectively to both support investment and return a fair share for the nation in normal circumstances, it is not designed for upwards price shocks and so will not achieve an adequate fair return for the nation in these circumstances. **To ensure a fair return for the nation at times of unusually high oil and gas prices the government will develop a new mechanism that could be used to respond to such price shocks post-2028, while also ensuring this happens in a more predictable way, in order to not deter investment. The introduction of such a mechanism should not be presupposed if prices rise. The government will need to consider a range of factors before deciding whether to introduce such a mechanism, including the economic and fiscal context of the day.**

2.11 The government has developed a set of principles for supporting investment which will inform the development of a future tax response to price shocks. These principles help give more certainty about the government's overall intentions whilst recognising the importance of allowing sufficient time beyond the end of the review to get the details right and that whether the mechanism is introduced will depend on a range of factors, including the economic and fiscal context of the day. Tax changes can often take years from initial design principles to being ready to roll out, given the technical nature, complex considerations and any legislative requirements. This is particularly so where tax changes are not based solely on existing tax structures. The government will continue to develop the design of a future mechanism and will continue to engage industry and update through fiscal forums.

2.12 The principles for responses to future price shocks are set out below:

- Respondents highlighted that clarity and predictability ahead of changes being implemented can allow better investment planning than making a wide range of potential assumptions about reactions to price shocks. While the EPL will end in March 2028 at the latest, the government is aware that the sector will need a clear plan for a future mechanism ahead of this, including how it defines a price shock and when it will be triggered in relation to this definition. **To support predictability, government will provide details on how price shocks will be defined in advance of the Energy Profits Levy ending and before a new mechanism is considered for introduction. The government recognises that by their nature oil and gas price shocks happen infrequently and are unexpected.**

- The government recognises that the design of a future mechanism can impact on investment decisions and welcomed the range of ideas highlighted about how to minimise impacts on investment, including suggestions for a future mechanism to focus only on the unexpected outcomes from price shocks and that a revenue-based tax may be preferable to a profits-basis. Tax designs to achieve this could be complex to develop, design and administer, so the government will want to consider these proposals in detail further. **If there are unexpected price shocks in future, then to support investment, a future mechanism would be targeted at the unexpected outcomes arising from a price shock in order to not impact investment decisions which are made assuming normal circumstances. When designing a future mechanism, the government will consider suggestions, such as assessing the benefits of capturing a share of revenue resulting from high prices, rather than profits.**

- During the Call for Evidence, respondents made it clear that if a future mechanism was introduced, they strongly welcomed a predictable approach. **Therefore, the government will hold regular engagement with stakeholders to understand the latest and evolving context for oil and gas investment, including a Ministerially chaired fiscal forum twice a year.**

2.13 While concerns around the EPL were made clear, Call for Evidence responses also highlighted that the permanent regime and its current investment incentives were viewed positively by industry and seen as fit for purpose. As noted in Chapter 3, respondents particularly noting the benefits of First Year Allowance and Investment Allowances and that they are an essential part of the fiscal regime in supporting investment decisions. The 2014 fiscal review[3] committed to reduce the tax burden from the industry – and this has already been delivered with the Supplementary Charge falling from 32% to 20% in 2015 and 10% in 2016. This supported maximising economic recovery of oil and gas resources in recognition of an increasingly mature basin, which was a key conclusion from the previous fiscal review. Maximising economic recovery is also set out in the NSTA's Strategy[4]. **In order to give certainty to industry, the government will also maintain the existing set of investment incentives in the permanent regime to support investment.**

Energy Transition and Decarbonisation

2.14 The government recognises the important role oil and gas infrastructure, skills and supply chains play in supporting the energy transition and deployment of low carbon technologies, including Carbon Capture, Utilisation and Storage (CCUS). **To support investment in low carbon technologies, the review confirms that the**

[3] Review of the oil and gas fiscal regime 2014, https://www.gov.uk/government/calls-for-evidence/review-of-the-oil-and-gas-fiscal-regime-a-call-for-evidence

[4] The OGA Strategy, NSTA, https://www.nstauthority.co.uk/regulatory-information/regulatory-framework/the-oga-strategy/

government will remove the tax barriers to oil and gas assets being repurposed for use in CCUS projects. The government will legislate in a future finance bill to introduce tax relief for payments made by oil and gas companies into decommissioning funds.

2.15 These payments will cover the oil and gas company's share of the decommissioning liability of the repurposed asset and be due tax relief of equal value to the relief available for ordinary decommissioning activities, levelling the playing field between decommissioning and repurposing and supporting the transfer of assets. After making a payment into a decommissioning fund, companies will be able to claim Change of Use Relief (CoUR), freeing them from any future decommissioning obligations in regards to the repurposed asset. Legislation will also remove receipts received from the sale of oil and gas assets which are repurposed for use in CCUS from the EPL, reducing the tax paid on this income from 75% to 40% ensuring EPL does not act as a disincentive for companies who support the transition.

2.16 **The government did not receive sufficient evidence on any other significant barriers to the energy transition in the oil and gas tax regime in order to justify further changes in the oil and gas tax regime. Given the energy transition and deployment of low carbon technologies building from the oil and gas sector is at an early stage, the government will continue to keep the role of the oil and gas fiscal regime under review as the transition progresses.** Autumn Statement also announces a generous permanent full expensing policy for those outside the oil and gas ringfence, helping to significantly boost capital investment and jobs in those sectors. That includes the development of the domestic supply chain for low carbon technologies, including CCUS.

2.17 To recognise the continued role of oil and gas in the energy system, balanced with the need for the sector to decarbonise to support net zero targets, government and industry committed to interim emissions reductions targets in the 2021 North Sea Transition Deal (NSTD). Through the NSTD, the sector has committed to reducing its emissions by 10% by 2025, 25% by 2027 and 50% by 2030, against a 2018 baseline. The NSTA estimates that while the sector is on track to meet the 2025 and 2027 NSTD emission reduction targets on its current trajectory, further abatement is required to meet the 2030 target. Key to delivering a 50% emissions reduction by 2030 will be eliminating routine flaring and venting, and electrifying platform operations.

2.18 To recognise the temporary higher rate of tax under the EPL, the Decarbonisation Allowance provides temporary, additional tax relief for decarbonisation investment and means overall relief is currently £1.0925/£. **To support the industry to decarbonise, the Decarbonisation Investment Allowance will remain in place for the duration of the EPL**.

2.19 **After the end of the EPL, the Decarbonisation Investment Allowance will end and the permanent regime will continue to offer tax relief of £0.4625/£ on investment, including for decarbonisation**.

The relatively lower value of tax relief available in the permanent regime will rightly reflect the lower rate of tax applicable after the end of the EPL.

2.20 The government recognises the diverse set of challenges faced by decarbonisation projects. It is vital the sector continues to deliver on decarbonisation commitments made in the NSTD. To support this, the NSTA has published a consultation on a draft Oil and Gas Authority plan to reduce UK Continental Shelf greenhouse gas emissions. The government has also published the Connections Action Plan setting out reforms to the grid connection process to ensure that the significant majority of applicants get the connection date they request with no delay. **The government will monitor progress against emissions reduction targets in the NSTD, assess the outcomes of the NSTA consultation and alongside maintaining investment allowances in the permanent fiscal regime, will consider options outside the scope of this Fiscal Review to encourage the sector to decarbonise if required, including the role of further carbon pricing.**

2.21 **The government will continue to engage stakeholders on the fiscal regime's interaction with energy transition and decarbonisation, including through discussion at fiscal forum meetings.**

Simplification

2.22 Simplifying the tax system reduces the time and money businesses and individuals spend on tax administration, helps boost productivity and supports growth. Following the closure of the Office of Tax Simplification, HM Treasury and HMRC were given a clear mandate to focus on simplicity of tax policy design throughout the policy making process and on simplifying existing tax rules and administration.

2.23 Overall, the permanent tax regime for oil and gas was viewed by CfE respondents as fit for purpose, with minimal suggestions for further simplification. Of suggestions made some also could have a net fiscal impact or change the fiscal profile, such as the removal of the need to activate Supplementary Charge investment allowances with relevant income. **The review concludes that the existing regime is effective, with limited scope for simplification changes.** Additionally, further simplification is not a main priority for industry, and large-scale change risks instability in the regime.

2.24 **The government will continue to engage with stakeholders to assess the benefits and costs of suggested changes**, with particular focus on changes that will improve companies' interaction with the regime, such as aligning the instalment payment dates for Ring Fence Corporation Tax (RFCT) and Supplementary Charge (SC) with Corporation Tax (CT), or future opportunities for change in the permanently zero-rated PRT regime. **This engagement will include discussion of these issues at fiscal forum meetings**. The government wants to ensure overall the tax system remains stable to support investment.

Conclusions

2.25 As set out above, the fiscal review confirms policy decisions and principles for future policy making. These are summarised below.

Supporting investment through predictability and certainty

2.26 To support predictability and certainty, the fiscal review confirms that the EPL will end in March 2028, or earlier if the ESIM is triggered.

2.27 To ensure a fair return for the nation at times of unusually high oil and gas prices the government will develop a new mechanism that could be used to respond to such price shocks post-2028, while also ensuring this happens in a more predictable way, in order to not deter investment. The introduction of such a mechanism should not be presupposed if prices rise. The government will need to consider a range of factors before deciding whether to introduce such a mechanism, including the economic and fiscal context of the day.

2.28 The government has developed a set of principles for supporting investment which will inform the development of a future tax response to price shocks. These are;

- To support predictability, government will provide details on how price shocks will be defined in advance of the Energy Profits Levy ending and before a new mechanism is considered for introduction. The government recognises that by their nature oil and gas price shocks happen infrequently and are unexpected.

- If there are unexpected price shocks in future, then to support investment, a future mechanism would be targeted at the unexpected outcomes arising from a price shock in order to not impact investment decisions which are made assuming normal circumstances rather than price shocks. When designing a future mechanism, the government will consider suggestions, such as assessing the benefits of capturing a share of revenue resulting from high prices, rather than profits.

- The government will hold regular engagement with stakeholders to understand the latest and evolving context for oil and gas investment, including a Ministerially chaired fiscal forum twice a year.

Energy Transition and Decarbonisation

2.29 To support investment in low carbon technologies, the review confirms that the government will remove the tax barriers to oil and gas assets being repurposed for use in CCUS projects. The government will legislate in a future finance bill to introduce tax relief for payments made by oil and gas companies into decommissioning funds.

2.30 The government did not receive sufficient evidence on any other significant barriers to the energy transition in the oil and gas tax regime in order to justify further changes in the regime at this time. Given the energy transition and deployment of low carbon technologies is at an early stage, the government will continue to keep the role of the oil and gas fiscal regime under review as the transition progresses.

2.31 To support the industry to decarbonise, the Decarbonisation Investment Allowance will remain in place for the duration of the EPL. After the end of the EPL, the Decarbonisation Investment Allowance will end and the permanent regime will continue to offer tax relief of £0.4625/£ on investment, including for decarbonisation.

2.32 The government will monitor progress against emissions reduction targets in the NSTD, assess the outcomes of the NSTA consultation on a draft Oil and Gas Authority plan to reduce UK Continental Shelf greenhouse gas emissions and alongside maintaining investment allowances in the permanent fiscal regime, will consider options outside the scope of this Fiscal Review to encourage the sector to decarbonise if required, including the role of further carbon pricing.

2.33 The government will continue to engage stakeholders on the fiscal regime's interaction with energy transition and decarbonisation, including through discussion at fiscal forum meetings.

Simplification

2.34 The review concludes that the existing regime is effective, with limited scope for simplification changes.

2.35 The government will continue to engage with stakeholders to assess the benefits and costs of suggested changes. This engagement will include discussion of these issues at fiscal forum meetings.

Overall conclusion

2.36 Together today's announcements on oil and gas show the government is committed in the short-, medium- and long-term to having a fiscal regime which supports investment in oil and gas sector. In the short-term, the next steps on ESIM provide clarity whilst the EPL remains in place. By confirming the EPL will end in March 2028 at the latest, the government provides certainty in the medium-term, and the fiscal review outcomes demonstrate the principles informing long-term tax design.

Chapter 3
Summary of responses

Respondents

The government is grateful to all respondents who took the time to engage with the Oil and Gas Fiscal Review, which has informed continued policy development.

The government welcomed around 50 written responses to the CfE, including from oil and gas industry, trade associations, providers of finance, renewables industry, and environmental groups. The government has considered the issues raised carefully and this chapter sets out an overview of the responses provided, which have been grouped and ordered to highlight the key themes of evidence received.

The Fiscal Regime and its context

The fiscal regime has been designed to encourage companies to explore for and develop the nation's oil and gas resources whilst aiming to ensure that an appropriate share of the benefits accrues to the UK economy as a whole. Since the start of offshore production in the mid-1960s the context of exploration and development has evolved significantly as the basin has matured and commercial practices have changed. Therefore, the CfE looked to expand the government's understanding of the changing context of oil and gas sector.

Question 4 - Net-zero, energy security and the predictability of the fiscal regime are discussed separately in the following chapters. Putting these contexts to one side, is there any additional context to oil and gas production and its future evolution that the Government should be aware of? Comparisons to the evolution of other mature basins are welcomed.

The CfE responses highlighted some additional context to the UK Continental Shelf (UKCS). For example, a changing ownership within the basin was noted, with an increasing role of private equity and state-owned enterprises entering the market. Some mentioned that this has increased commercial risk, including due to challenges in raising finance.

In addition, a strong message from the oil and gas sector was that the Energy Profit Levy (EPL) is impacting the long-term stability of the regime, due to concerns that it will be extended further.

However, environmental group countered this, raising concerns that the current fiscal regime is not well balanced towards returns for the nation.

Some comparisons were made between Norway and the UK, noting that Norway has seen more investment and development in recent years. However, it was also noted that comparisons are difficult to make, due to fields being larger and the geology being simpler in Norway.

Investment focused on oil and gas production

The investment context will continue to evolve as the UK's basin matures and market conditions change, with the fiscal regime an important consideration in investment decision making. Therefore, the CfE sought to gather information, so that the government could understand the different factors influencing investment, how businesses evaluate the economics of a project, and how those project economics are changing as the UK basin matures.

Oil and gas investment context

Question 5 - What are the main factors that influence investment decisions in a stable fiscal regime?

Most upstream oil and gas producers raised that fiscal stability in the UK is a key influencer in making investment decisions. Many noted their view that the number of changes without prior warning have been particularly harmful, especially when the UK is compared to international opportunities. Because of this, a large number of responses from upstream producers highlighted an interest in the future fiscal regime giving more predictability and stability.

Other key factors raised by upstream producers that influence investment decisions included risk appetite, profitability, regulatory risk and the availability of capital. However, many responses were clear that fiscal predictability and stability came above these and was seen as more of a factor than the level and structure of current investment allowances.

Oil and gas supply chain industry responses mirrored a number of the same concerns as upstream producers, adding that a steady and predictable flow of contract awards impacts investment, which in turn is also impacted by fiscal instability.

On the other hand, environmental groups noted that, as the UK is a mature basin, it results in higher costs. Therefore, their view was that the focus should be managing the decline of oil and gas production, rather than investing further. This view resulted in asks that government should provide predictable and clear transition planning for the sector, in order to support the energy transition.

Question 6 - When evaluating the economics of a project, what metrics and / or hurdle ratios are used?

Question 7 - How do you expect the economics of UK projects to evolve over the coming decades, including new and incremental investments? How might these economics vary on project scale and type?

Industry shared that a number of conventional metrics, primarily Net Present Value, Internal Rate of Return and payback periods, are used to assess the economics of a project, which are affected by a combination of factors including costs, fiscal terms and risks. Comments on evaluating project economics included relatively limited detail, noting concerns around confidentiality. However, it was clear that a combination of metrics are used, and this varies between companies.

Respondents noted a general theme of declining investment over time as the UKCS matures, due to projects becoming more marginal, as costs increase, shared infrastructure is spread more thinly, and capital becomes more difficult to obtain.

However, some upstream producers noted potential opportunities for some project economic positives, due to use of technology and the use of fields for CCUS and renewables, noting that there is a high level of uncertainty in these areas.

Question 8 - Over the coming decades, how will the UK typically compare to other oil and gas investment opportunities globally in other mature basins?

Overall, most respondents did not see the UK as currently competitive compared to other mature basins, due to the fiscal instability outlined above, complex technical difficulties due to the maturity of the basin and higher costs.

However, upstream producers and supply chain businesses noted their view that the energy transition is heavily reliant on the oil and gas industry and its skills and infrastructure and emphasised the need to support the industry through the tax regime to aid this.

Changes to the tax regime that incentivise the development of CCUS and integrated energy hubs, including offshore wind and hydrogen production in the North Sea, were suggested as a way to ensure the UK is an attractive destination for international investment.

The fiscal regime

Question 9 - Which elements of the current fiscal regime have incentivised investment in the UKCS? What elements if any have discouraged investment?

Question 10 - How have existing capital allowances influenced decisions to invest in the UKCS and how important is this in comparison to other investment incentives? Is the capital allowances regime for ring-fence activity fit for purpose?

Question 11 - Are there elements of project expenditure that don't currently qualify for relief under the existing allowances? Are there any elements which should no longer be included as they reflect historical and not future practice?

Overall, oil and gas operators shared positive views of the current permanent regime and its existing allowances, particularly noting the benefits of First Year Allowance and Investment Allowances and that they are an essential part of the fiscal regime in supporting investment decisions. During engagement, some operators asked whether contractual certainty could be given by the government in order to support investment further, particularly noting the benefits of Decommissioning Relief Deeds.

However, most oil and gas industry responses noted that the EPL makes the UKCS uncompetitive globally. Some operators highlighted the cyclical nature of oil and gas production and that many operators balance the economics of a project across the high and low-price scenarios over time. Oil and gas supply chain operators also highlighted the impact of high headline tax rates further down the supply chain and this risked work moving overseas.

Some new entrant challenges were also noted, particularly where those without existing oil and gas tax history cannot immediately offset their costs, whereas established/producing operators can currently offset their investment expenditure against existing revenues.

Some respondents highlighted interest in using allowances in the oil and gas ringfence for low carbon projects. Others suggesting setting costs from low carbon projects off against oil and gas profits to reduce oil and gas taxes.

Stability and predictability

The government recognises that stability in the tax regime plays an important role in influencing investment decisions. It is also important, however, that the government strikes a balance between attracting investment and ensuring the nation receives a fair return on the exploitation of its natural resources. The review therefore explored questions around how the future fiscal regime responds to price shocks, following the end of the EPL in March 2028 (or earlier, if prices fall below Energy Security Investment Mechanism (ESIM) levels).

Question 20 - What are your long-term projections for oil and gas prices? What prices would be above usual profit-making assumptions, and what drivers for higher prices do you foresee?

Question 21 - Do you think in the long term the fiscal regime should have a clear mechanism for responding to future price shocks? If so, what principles should the government consider in relation to this?

Most upstream producers did not support a pre-set mechanism for tax to respond to price shocks and called for the removal of EPL in their CfE responses, noting concerns that the government may extend the EPL, or introduce a similar mechanism, post-2028. However, some were more positive about a predictable revenue-based regime in engagement sessions. Some also flagged that the benefits of higher commodity prices can be reduced in an inflationary cost environment.

Of the upstream producers who were accepting of the need for a price shocks mechanism, they strongly welcomed the government taking an open and consultative approach in order to provide industry with predictability and foresight of any changes. They also made some design suggestions, including that any price trigger is reflective of profitability, basin maturity, the high-cost nature of industry and based on real prices rather than nominal.

Some upstream producers commented that long term policy should not be set on unexpected price shocks, noting that the risk of investing is managed through regular high and low-price cycles. A number of upstream producers highlighted the price shocks can also happen downwards and asked that government give predictability both on the upside and downside.

Environmental groups called for the EPL to be made permanent at a higher rate and investment incentives to be removed. The oil and industry have shared strong concerns around the EPL and impacts on investment if it were to be extended.

Investment in oil and gas to support energy security

A key objective of the fiscal regime is to support oil and gas production, helping energy security and ensuring low carbon technologies can leverage existing skills and supply chains to accelerate their growth. Therefore, the CfE sought views on the scale to which oil and gas will contribute to energy security over the coming decades.

Question 12 - What evidence do you have on the scale of oil and gas investment opportunities to contribute to UK energy security over the coming decades? How will this contribution vary across different types of investment e.g. investment in new developments, incremental investment in existing developments?

Responses from those in the oil and gas sector highlighted the ongoing UK energy demand for oil and gas in the coming decades and that investments in oil and gas production could help meet that need and limit the need to depend on imported oil and gas. There was a range of views about the scale of remaining recoverable reserves in the UK and discussion about how recoverable reserves were lower than total reserves given some extraction was not feasible or economic. There was also limited detailed commentary about how the scale of these reserves translated into energy security benefits. Some responses highlighted the differential investment needs from new developments and incremental projects.

Responses from environmental groups suggested there were limitations to the scale of energy security benefits from oil and gas investment. This included noting views about the shares of domestic oil and gas production which are typically exported, limited impact on energy affordability of domestic production and oil and gas competition with renewable energy generation making such generation more challenging.

Investment to support decarbonisation and the transition to net zero

As the UK transitions to net zero, oil and gas will retain a crucial role in the energy system, until there are sufficient renewable alternatives. In 2021, the government agreed the North Sea Transition Deal (NSTD) with the sector. Through the NSTD, the UK's oil and gas sector and the government will work together to deliver the skills, innovation and new infrastructure required to decarbonise North Sea oil and gas production, as well as moving forward on hydrogen, on CCUS, and on offshore renewables.

To support the sector to decarbonise, the permanent oil and gas fiscal regime offers investment allowances of £0.4625/£. In January 2023 the EPL decarbonisation investment allowance (DIA) was introduced to provide total relief on decarbonisation investment of £1.0925/£, in recognition of the temporary higher rate of tax under the EPL.

The government sought views on the role of the future long-term role of the fiscal regime in decarbonisation of oil and gas production and supporting the growth of offshore low carbon technologies.

Decarbonising oil and gas production

Question 13 - What do you see as the main obstacles / barriers to decarbonising existing and future production in the UK?

Question 14 - To what extent does the fiscal regime influence decarbonisation of production in the UK? How does this interact with other influences on decarbonisation, including the UK Emissions Trading Scheme?

Question 15 - In the long term, how do you think UK production emissions from oil and gas will compare to other production globally and will this vary over time?

Most respondents called for greater certainty over the long-term policy framework, to support decarbonisation. Respondents from the oil and gas industry called for more certainty over future tax and regulatory policy to support long term investment decisions, whereas environmental groups called for clearer policy signals on the phase out of fossil fuels.

The regulatory regime (including licencing requirements and grid connections), technical challenges and high costs were cited by respondents from the oil and gas industry as barriers to oil and gas decarbonisation projects.

Many respondents from the and oil and gas industry welcomed the introduction of the DIA as a positive step in supporting decarbonisation projects to go ahead, in the context of higher tax rates under the EPL. There were some calls to make the DIA a permanent part of the regime once the EPL ends and for the government to expand the scope of the DIA. However, there was also a suggestion that the main driver to decarbonise is North Sea Transition Deal (NSTD) targets and maintaining a 'social licence to operate', rather than fiscal incentives.

There were mixed views overall on the impact of the UK Emissions Trading Scheme (ETS). Some respondents said that the UK ETS helps to incentivise decarbonisation, whereas others said the volatility and level of the ETS price meant it had a limited impact on long-term investment decisions. Some oil and gas trade bodies and producers called for methane to be included in the scheme and one trade body suggested the government should consider alignment with the EU ETS.

Most respondents speculated the UK will continue to outperform global averages on emissions from oil and gas production, due to strong regulatory oversight, targets to reduce emissions in the NSTD and strong societal imperative to reduce emissions.

Oil and gas industry respondents said that the targets in the NSTD were likely to be met with government support, while environmental groups called for more action noting their view that the UK does not perform as well on emissions from production as other mature basins, such as Norway.

Supporting the energy transition and road to net zero

The oil and gas sector have highly transferable infrastructure, skills and supply chains which have the potential to play an important role in the growth of low carbon technologies and transition to clean energy. The CfE sought to understand these issues and the impact of the oil and gas tax regime on them.

Question 16 - To what extent do you think future lower carbon projects will be dependent on the existing fossil fuel infrastructure and skill base?

Question 17 - Increasingly both oil and gas and other sectors are becoming involved in lower carbon technologies. What are the main barriers within the fiscal regime to the repurposing of assets for the deployment of lower carbon technologies? How does the oil and gas fiscal regime compare to the non ring-fence regime in respect of lower carbon technologies?

Question 18 - How does the prospect of assets being repurposed in the deployment of lower carbon technologies in the long-term influence current investment decisions and the economics of projects?

Many respondents commented that low carbon technology projects would be highly dependent on leveraging the existing highly skilled workforce. It was also noted that there are risks of talent drain, both outside the sector or to overseas markets, if investment in low carbon technology projects does not materialise. It was also noted that many roles are highly transferrable to offshore low carbon technology projects.

Many respondents viewed existing upstream oil and gas infrastructure as likely to be vital for CCUS in particular – but they viewed it as less clear that wind, green hydrogen or solar will directly use this infrastructure. Some respondents noted that not all oil and gas infrastructure is suitable to be repurposed.

Respondents called for tax technical changes to encourage the repurposing of oil and gas assets to be used in CCUS. There were calls for more certainty on the tax treatment of decommissioning costs for repurposed assets previously used in the ringfence and treatment of future contributions to decommissioning funds. Respondents also noted also that policy, fiscal and regulatory stability and certainty are also required alongside supportive tax treatment. Beyond the tax technical change to support reuse of assets, limited barriers to the energy transition and roll out of low carbon technologies, within the scope of the oil and gas fiscal regime, were identified by respondents.

Environmental groups and some respondents from the renewables sector said the government should offer more targeted investment incentives for the renewables sector, such as targeted capital allowances. Environmental groups said the government should remove the DIA and instead focus incentives on renewables projects that supply energy to the national grid.

Upstream producers generally indicated that as repurposing is in its infancy with unknown costs and benefits, it does not factor into investment decisions.

Simplicity

Simplifying the tax system reduces the time and money businesses spend on tax administration, helps boost productivity and supports growth. HM Treasury have a clear mandate to focus on simplicity of tax policy design throughout the policy making process and on simplifying existing tax rules and administration where it makes sense to do so.

Question 19 - Are there aspects of the fiscal regime that could be simplified in a revenue neutral way overall? If so, what are they and what would the benefits and costs be of implementing the necessary changes.

Most respondents to this question were oil and gas companies who were familiar with the workings of the tax regime. Many respondents took the opportunity to call for the removal of EPL as a simplification measure, or to make suggestions that didn't fit with the overall revenue neutrality requirements. No quantitative evidence was provided on the benefits or costs of any changes.

While there was general support for a simplification agenda, a large number of respondents noted that on the whole, the permanent regime was fit for purpose, or that simplification was not a priority when compared to stability.

There was a mixed response to the suggestion raised in the CfE of a possible closer alignment between RFCT and SC. Although there was some support that may simplify the regime, most respondents noted that the regime was well understood and functional.

The most popular smaller change suggested was removal of the need to activate SC investment allowances with relevant income before relief can be provided, which was suggested multiple times. Some respondents viewed this change as one also related to investment. A small number of respondents supported the suggested changes to PRT filing dates and requirements, and potential changes to the instalment payment schedule for ringfence taxes, bringing payment dates in line with the existing schedule for Corporation Tax. This change has the potential to reduce administrative burden on companies who may be required to make seven payments a year across both regimes.

Equalities

Question 22 - If not covered by your answers to other questions, what are in your view the implications of these policy considerations for those who share a protected characteristic? If there are negative impacts, what potential mitigations could be considered?

Most respondents did not provide a response to this question. However, civil society groups did call for the energy transition to be equitably designed based on principles of justice.

Next steps

The government has now considered the responses submitted in the Call for Evidence, the outcomes and next steps of which are outlined in Chapter 2 of this document.

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This document can be downloaded from www.gov.uk

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