UK Tax Policy in the Oil and Gas Sector: An Empirical Examination of Recent Changes

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Abstract

The UK oil and gas industry is past maturity, with an ageing infrastructure. The UK North Sea Transition Authority (NSTA, formerly, the Oil and Gas Authority (OGA)) has set Maximising Economic Recovery as a key objective for operators. This aims to preclude the decommissioning of mature fields by transferring ownership of late-life oil/gas assets to independent, smaller firms capable of operating them at reduced costs, thus extending the lives of these assets. Such transfers are complicated by policies concerning the tax capacity of the buyer; the transferability of tax history between operators; the issue of a "no clean break" between operators and government; the functioning of decommissioning tax relief; the risk that smaller operators' ultimate failure to decommission may result in costs falling upon the UK Government, hence on taxpayers; and recent commitments to "net zero" carbon emissions. This article examines the effect of the decommissioning tax relief and transferability of tax history policy mechanisms on decommissioning late-life oil/gas assets on the UK Continental Shelf (UKCS) or extending their lives by way of the transfer of ownership. Utilising semi-structured interviews to obtain empirical data, the authors conclude that transferring ownership between operators Maximises Economic Recovery, contributes to revenue and does not expose taxpayers to potential decommissioning costs. However, the fairness of the UK petroleum fiscal regime, and in particular the administration of decommissioning tax relief, appears questionable.

(1) Introduction

Although it is now over 50 years old, the UK oil and gas sector still provides about half of the UK's primary energy needs.[1] It supports over 300,000 jobs and contributes to the public purse via taxation.[2] The net amount of revenue received in 2019–20 was £863 million,[3] which is a substantial amount of

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[1] Department for Business, Energy and Industrial Strategy and the Prime Minister's Office, *Policy Paper—British Energy Security Strategy* (TSO, 2022), *https://www.gov.uk/government/publications/british-energy-security-strategy/british-energy-security-strategy* [Accessed 8 September 2022].

[2] HMRC, *Policy Paper—Oil and Gas Taxation: Transferable Tax History and Retention of Decommissioning Expenditure* (TSO, 2020), *https://www.gov.uk/government/publications/oil-and-gas-taxation-transferable-tax-history-and-retention-of-decommissioning-expenditure/oil-and-gas-taxation-transferable-tax-history-and-retention-of-decommissioning-expenditure* [Accessed 8 September 2022].

[3] HMRC, *Statistics of Government Revenues from UK Oil and Gas Production* (TSO, 2020), *https://www.gov.uk/government/statistics/government-revenues-from-uk-oil-and-gas-production--2* [Accessed 8 September 2022]. Table 11.11, Government revenues from UK oil and gas production 1968–69 to 2019–20 shows that the £863 million is made up of ring fence corporation tax (RFCT) of £1,156 million, plus supplementary charge (SC) of £254 million, less repayments of £136 million, less petroleum revenue tax (PRT) repayments of £411 million. See section 2 of this article for further details.

money in terms of tax take. Although an estimated 20 billion barrels of oil remain,[4] oil and gas production has passed its peak. An ageing infrastructure, which is now over 50 years old, high taxes, increased operating costs and the fluctuations in oil prices[5] have created serious difficulties.[6] The maturity of the UK oil and gas industry has led to a number of oil fields being subject to abandonment and therefore to the risk of losing a significant amount of the UK national oil and gas wealth.[7] The UK North Sea Transition Authority (NSTA) (formerly, the Oil and Gas Authority (OGA))[8] believes that, with improving management of existing wells and suitable intervention mechanisms, the closure rate will slow down and production from marginal wells will be able to be maximised, an objective that was set by a commissioned review conducted by Sir Ian Wood in 2014, reiterated by the OGA, and termed Maximising Economic Recovery.[9] As smaller oil and gas operators experience lower overheads than the very large firms (for example, Shell, BP, Exxon Mobil, Total, Chevron and Eni, commonly referred to as "super majors") and offer greater specialisation, they often incur lower operating costs in extracting oil and gas from smaller and marginal fields.[10] There is therefore a strong case for transferring such fields from existing larger operators to smaller firms to maximise economic recovery from them.

In 2019, however, the UK Government introduced legislation which requires the UK to bring all greenhouse gases to "net zero" by 2050.[11] "Net zero" means that any emissions should be offset by schemes to remove an equivalent amount of greenhouse gases from the atmosphere (for example, planting trees or capturing and storing carbon). Such legislation is expected to have a material impact on the UK oil and gas industry and its stakeholders[12]: significant reductions in greenhouse gas emissions

[4] World Oil, "UK projects up to 20 billion barrels of oil remain to be found offshore" (14 September 2020), *https://www.worldoil.com/news/2020/9/14/uk-projects-up-to-20-billion-barrels-of-oil-remain-to-be-found-offshore#:~:text=UK%2FUKCS-,UK%20projects%20up%20to%2020%20billion%20barrels,remain%20to%20be%20found%20offshore&text=Connect%20with%20World%20Oil%2C%20the,into%20operational%20and%20technological%20advances* [Accessed 8 September 2022].

[5] For the first time in history, US oil prices became negative during the Covid-19 pandemic (see Sarah Hansen, "Here's what negative oil prices really mean", *Forbes*, 21 April 2020, *https://www.forbes.com/sites/sarahhansen/2020/04/21/heres-what-negative-oil-prices-really-mean/#545f09955a85* [Accessed 8 September 2022]). Negative oil prices mean that oil and gas companies paid traders for taking their produced oil (see Andrew Walker, "US oil prices turn negative as demand dries up" (*BBC News*, 21 April 2020), *https://www.bbc.co.uk/news/business-52350082* [Accessed 8 September 2022]). Brent oil price reached $19/barrel in April 2020, down from $68/barrel in January 2020.

[6] Sir Ian Wood, *UKCS Maximising Recovery Review: Final Report* (TSO, 2014), *https://www.nstauthority.co.uk/media/1014/ukcs_maximising_recovery_review.pdf* [Accessed 8 September 2022].

[7] Michael Davar and Gideon Shirazi, "Decommissioning in the UK Continental Shelf: A litigator's perspective" [2015] I.E.L.R. 192; Oil & Gas UK, *Decommissioning Insight 2016* (London: Oil & Gas UK, 2016), *https://cld.bz/bookdata/jb05Hxr/basic-html/page-1.html* [Accessed 8 September 2022].

[8] The OGA changed its name with effect from 22 March 2022. In this article, therefore, the authors refer to NSTA where the context is current, and OGA where it is historic. The change of name affects many of the internet addresses for documents accessed, so the authors have retained the address that was current when these documents were accessed by them.

[9] Wood, *UKCS Maximising Recovery Review: Final Report* (2014); Greg Gordon, John Paterson and Uisdean Vass, "The Wood Review and Maximising Economic Recovery upon the UKCS" in Greg W. Gordon, John B. Paterson and Emre Üşenmez (eds), *UK Oil and Gas Law: Current Practice and Emerging Trends: Vol. I: Resource Management and Regulatory Law*, 3rd edn (Edinburgh: Edinburgh University Press, 2018), p.133.

[10] Virginia Parente et al, "Offshore decommissioning issues: Deductibility and transferability" (2006) 34(15) *Energy Policy* 1992.

[11] Department for Business, Energy and Industrial Strategy and The Rt Hon. Chris Skidmore MP, press release, *UK becomes first major economy to pass net zero emissions law* (27 June 2019), *https://www.gov.uk/government/news/uk-becomes-first-major-economy-to-pass-net-zero-emissions-law* [Accessed 8 September 2022].

[12] "Calls for 'reasoned debate' over oil and gas future" (*BBC News*, 19 December 2021), *https://www.bbc.co.uk/news/uk-scotland-scotland-business-59717784* [Accessed 8 September 2022].

imply significant reductions in consumption and production of oil and gas.[13] Despite "net zero" being anticipated as "a smooth transition, not an immediate extinction, for oil and gas",[14] transitioning to "net zero" is likely to result in decommissioning or abandonment of oil and gas assets.[15] Against this backdrop, oil and gas companies are facing tough business options: selling their oil and gas assets or changing their investment portfolio to include more renewable energy options at the expense of oil and gas investments.[16] Therefore, transferring late-life assets to smaller and more cost-efficient companies seems a good solution for larger companies with an international investment portfolio who may want to move away from the UK Continental Shelf (UKCS)[17] and to smaller companies who may be looking for investment opportunities on the UKCS. However, since the UK Government has recently introduced an energy profits levy (EPL) of 25 per cent on profit generated by oil and gas companies in the UK, smaller companies may find it hard on the one hand, to make sufficient profit and, on the other, to pay for decommissioning retired assets. Therefore, UK oil and gas companies seem to be subject to "push" and "pull" factors in terms of their investments. Whilst enhanced oil and gas prices, transferability of tax history and the Maximising Economic Recovery objective are "push" factors for enhanced investments and transferability of assets between operators, "net zero" legislation (given particular prominence by the United Nations Climate Change Conference, COP26, held in Glasgow between 31 October and 13 November 2021), the EPL, and the instability and complexity of the UK petroleum fiscal regime are "pull" factors, and may discourage transfer of assets between operators. However, owing to the unbalanced energy market and threats to energy security because of the Russia-Ukraine war, premature shutting down of oil and gas fields may not be allowed: the UK Government is due to release a new oil and gas exploration licencing round in the autumn of 2022. This is mainly to meet the short-term energy security requirements of the country.[18]

The abandonment or decommissioning of oil and gas installations has, however, long been an issue of concern, highlighted especially by the dumping of the Piper Alpha rig into the North Sea following its destruction in an explosion in 1988—a precedent which Shell (then supported by the British Government) tried to follow in 1995 in its abortive attempt to dispose of the Brent Spar platform in deep water in the North Atlantic.[19] Greenpeace's protests over the latter were an early indication of environmental concerns about oil and/or gas platform disposals, which concerns were also raised by academic commentators, along with questions about the costs of disposals, whether the UK Government would provide any assistance in meeting those costs, and what the accounting and tax implications of abandonment might be.[20]

The UK petroleum fiscal regime, regulated by the UK Continental Shelf Act 1964, provides a decommissioning tax relief for the decommissioning costs of oil and gas assets. To prevent premature closure and allow smaller operators to use their specialised skills in extracting oil from mature fields, thus achieving its Maximising Economic Recovery objective, and to enhance further the effectiveness of decommissioning tax relief, the UK Government introduced legislation in the Finance Act 2019 (FA 2019) that allows transferability of tax history between operators, along with the transferability of ownership of late-life oil and gas assets. In essence, this means that a seller of a UKCS oil and gas

[13] Gordon Nardell KC and Maria Kennedy, "Offshore decommissioning: Zeroing in on trends and challenges", *Twenty Essex, Bulletin*, April 2021, *https://www.twentyessex.com/wp-content/uploads/2021/04/Decommissioning-of-oil-and-gas-platforms.pdf* [Accessed 8 September 2022].
[14] Department for Business, Energy and Industrial Strategy and the Prime Minister's Office, *British Energy Security Strategy* (2022).
[15] Gregor Semieniuk et al, "Stranded fossil-fuel assets translate to major losses for investors in advanced economies" (2022) 12 *Nature Climate Change* 532.
[16] Antony Seely, *Taxation of North Sea Oil and Gas* (TSO, 2022), Research Briefing, House of Commons Library, *https://commonslibrary.parliament.uk/research-briefings/sn00341/* [Accessed 8 September 2022].
[17] Seely, *Taxation of North Sea Oil and Gas* (2022).
[18] Fiona Harvey, "UK to defy net zero targets with more oil and gas drilling", *The Guardian*, 6 April 2022, *https://www.theguardian.com/environment/2022/apr/06/uk-more-oil-gas-drilling-north-sea-energy-security-strategy-kwasi-kwarteng-net-zero-targets?CMP=twt_a-environment_b-gdneco* [Accessed 8 September 2022].
[19] Alex Russell, Reza Kouhy and Robert Lyon, *Accounting for the Abandonment of North Sea Oil and Gas Wells* (London: Certified Accountants Educational Trust, 1998), pp.1, 3.
[20] Russell, Kouhy and Lyon, *Accounting for the Abandonment of North Sea Oil and Gas Wells* (1998).

interest can transfer part of its tax history to the buyer, such that the buyer may be able to use losses arising on decommissioning to trigger a repayment of taxes paid in previous years, which hitherto could only have been claimed had the assets remained in the hands of the original developer. The new regime is elective, complex, and applies to transfers on or after 1 November 2018.

There is a lack of studies on UK oil and gas taxation, which is perhaps surprising given the importance of the use of fossil fuel and its contribution to global warming and the UK's pledge to reduce greenhouse gases and emissions to "net zero" by 2050. The impact of both decommissioning tax relief and the transferability of tax history legislation on the decommissioning or transferring of ownership of late-life oil and gas assets on the UKCS, and thus on Maximising Economic Recovery from these assets, has therefore not been addressed. It is this gap that has given rise to this article, which is also motivated by particular considerations of relevance to UK Government tax policy. In the first instance, the extent to which both decommissioning tax relief and the transferability of tax history have, initially, provided solutions or created barriers to the transfer of late-life oil and gas assets is unknown. Similarly, the extent to which the transferability of tax history impacts on Maximising Economic Recovery, and thus enhances the social, financial, and economic objectives of the UK Government, is also unknown. There have also been concerns about the financial ability of low cost operators who may buy late-life assets from the major operators to decommission these assets in due course if they cannot sell them, thus generating the fear that liabilities for such decommissioning would default to the original owners of such fields, who might no longer have any business on the UKCS, and so would fall back on the UK Government, and hence on taxpayers. Hence this creates a potential cause of disquiet for the general public. In addition, there are concerns about the perception and overall fairness of the UK tax system as regards oil and gas taxation. Companies are not permitted to offset against their taxable profits provisions for decommissioning costs (in whole or part) in the form of depreciation. In order to claim decommissioning tax relief, decommissioning costs must have been paid for, not merely accrued. This means that, effectively, by the time of decommissioning, oil and gas companies will have paid more tax than they actually owed if the decommissioning costs are taken into account as accruing over time. Therefore, paying for decommissioning, before becoming entitled to claim decommissioning tax relief, creates pressure on oil and gas companies' cash flow. This raises a further query about the extent to which the decommissioning tax relief is a tax refund or a cost to the UK taxpayer, an issue that seems to have been misinterpreted recently by a number of media voices.[21]

While there is a wealth of governmental, non-governmental and industry documentation on oil and gas taxation (such as that issued by the NSTA/OGA, Gov.UK, the Department for Business, Energy and Industrial Strategy, the Department of Energy and Climate Change, HMRC, HM Treasury, Parliament.UK, also Oil & Gas UK, as well as relevant statutes/conventions, notably the Continental Shelf Act 1964, the Petroleum Act 1998, Capital Allowances Act 2001 (CAA 2001), FA 2019 and the United Nations Convention on the Law of the Sea (UNCLoS) as well as Sir Ian Wood's report, *UKCS Maximising Recovery Review: Final Report*, referred to earlier), the academic literature on the topic of UK offshore decommissioning taxation is scarce in the extreme. The only relevant study found to date was that undertaken by Parente et al, "Offshore decommissioning issues: Deductibility and transferability",[22] in which the deductibility of decommissioning expenses and the transferability of oil and gas projects among operators were considered. Parente et al contended that, should a government want to enhance recoverability from its marginal oil and gas fields, a suitable fiscal regime is needed that incentivises transferability of such assets between operators and incentivises smaller operators to

[21] Tom Baxter, "Why is decommissioning not a cost to taxpayer?" (*Energy Voice*, 14 November 2019), *https://www.energyvoice.com/opinion/212048/why-is-decommissioning-not-a-cost-to-the-taxpayer/* [Accessed 8 September 2022]; Mark Williamson, "North Sea oil and gas decommissioning cost estimate cut by billions amid efficiency drive", *The Herald*, 3 July 2019, *https://www.heraldscotland.com/business_hq/17745140.north-sea-oil-and-gas-decommissioning-cost-estimate-cut-by-billions-amid-efficiency-drive/* [Accessed 8 September 2022]; Adam Vaughan, "British taxpayers face £24bn bill for tax relief to oil and gas firms", *The Guardian*, 25 January 2019, *https://www.theguardian.com/business/2019/jan/25/british-taxpayers-bill-tax-relief-oil-gas-companies* [Accessed 8 September 2022].

[22] Parente et al, "Offshore decommissioning issues: Deductibility and transferability" (2006) 34(15) *Energy Policy* 1992.

invest in such fields. The current article extends this literature by focusing on the UK case. The authors investigate both the impact of decommissioning tax relief and the transferability of tax history on Maximising Economic Recovery and the fairness of the decommissioning tax relief and the transferability of tax history legislation in relation to the oil and gas companies and taxpayers.

The significance of this article emerges from the concerns raised above. Addressing such concerns is key first of all for the UK Government as the results of so doing offer an assessment of both the policy underpinning the transferability of tax history legislation and its impact on the Maximising Economic Recovery objective. Further, this article is of particular importance to the oil and gas industry which needs to realise the significance of the Maximising Economic Recovery objective. It is also important to UK taxpayers who need to know the potential extent of their exposure and resulting contribution to the decommissioning costs of oil and gas assets. In addressing these concerns and aims, this article raises the following specific questions:

1) To what extent does the current UK petroleum fiscal regime affect transfers of ownership of late-life oil and gas assets between operators on the UKCS?

(a) What impact do decommissioning tax relief and the transferability of tax history have on ending or extending lives of oil and gas fields on the UKCS?
(b) What barriers may prevent the transfer of late-life oil and gas assets between operators on the UKCS?
(c) What risks may the Exchequer incur as a result of an enhanced transfer of late-life assets on the UKCS? If there are any such risks, how can they be dealt with?
(d) What benefits does the transfer of ownership of late-life assets on the UKCS bring to the Exchequer?

2) What impact would the transfer of late-life assets have on Maximising Economic Recovery?

3) What impact would Maximising Economic Recovery have on UK petroleum tax revenues?

4) What other tax reform could be offered by the UK Government to delay decommissioning late-life oil and gas assets and encourage transfer of these assets between operators?

5) Is the decommissioning tax relief perceived as a government contribution towards decommissioning costs of oil and gas assets or a tax refund for tax overpaid by oil and gas companies?

The remainder of this article is structured as follows. Section 2 considers the history of the UK petroleum fiscal regime, with section 3 going on to address in greater depth the more current issues referred to above, with both sections drawing on the governmental, non-governmental and industry documents referred to earlier. The methodological approach is presented in section 4. Section 5 presents the analysis of the interview data and section 6 concludes.

(2) History of the UK petroleum fiscal regime

The first legal foundations of the UK petroleum fiscal regime were established by the Petroleum (Production) Act 1918, the objective of which was to control exploitation of UK petroleum resources. This Act was repealed and replaced by the Petroleum (Production) Act 1934 (the 1934 Act) which regulated the granting of licences to explore for and exploit petroleum resources in Great Britain.[23] The 1934 Act allowed licences to be issued "to search and bore for and get petroleum",[24] "for such

[23] HMRC, Internal Manual, *Oil Taxation Manual* (TSO, 2016; updated 22 December 2021), "OT00040—The taxation of the UK oil industry: An overview: Legal overview 1918 to Petroleum Act 1998", *https://www.gov.uk/hmrc-internal-manuals/oil-taxation-manual/ot00040* [Accessed 8 September 2022].
[24] Petroleum (Production) Act 1934 s.2(1).

consideration (whether by way of royalty or otherwise)"[25] as may be determined with the consent of the Treasury. In 1964, the licensing regime was extended to the UKCS by the Continental Shelf Act 1964 with a 12.5 per cent royalty on production. Since its original establishment, the UK petroleum taxation regime has been subject to many changes.[26] The regime's resultant instability and the uncertainty arising from future changes that could, potentially, affect it would easily deter investments in the UKCS.[27]

Successive administrations have developed a fiscal regime that operates under a concession system. This regime aims to provide taxation incentives to oil and gas companies to explore and develop the UK's oil and gas resources, and thus maximise economic recovery by using these assets, while at the same time securing a fair return on these resources for the nation.[28] The governance of this fiscal regime has been described as being non-proprietorial.[29] One aspect of the non-proprietorial regime is to not leave a unit of oil and/or gas production in the ground as long as it is profitable to extract it,[30] which meets the Maximising Economic Recovery objective of the NSTA.[31]

The current UK petroleum fiscal regime consists of four different taxes: ring fence corporation tax (RFCT)[32] at 30 per cent, a supplementary charge (SC) at 10 per cent (which together are referred to as "offshore corporation tax"), a petroleum revenue tax (PRT) set permanently to 0 per cent, and the recently introduced energy (oil and gas) profits levy (EPL) at 25 per cent.[33] The SC is an additional charge to the RFCT and is levied on a company's ring-fenced profit and is applicable to the same calculated profit as RFCT but without any deduction for financing costs. The EPL takes effect for accounting periods beginning on or after 26 May 2022 and applies to the same tax base as SC except that losses incurred prior to its introduction are not brought into account.[34] Petroleum revenue tax, which is a field based tax applicable only to fields given development consent prior to 16 March 1993, is retained so that losses, especially those resulting from the cost of decommissioning those fields, can be carried back against past profits subject to PRT thus triggering PRT repayments (with capped interest).[35] The authors consider the various taxes in more detail below.

(a) Petroleum revenue tax (PRT)

In the early 1970s, a significant number of discoveries was made in the UK North Sea.[36] Coupled with the significant increase in oil prices due to the 1973 Arab-Israeli war, these discoveries prompted the UK Government to introduce PRT in the Oil Taxation Bill 1974 at a rate of 45 per cent.[37] The Bill became the Oil Taxation Act 1975. Petroleum revenue tax was introduced on a cash flow basis, but

[25] Petroleum (Production) Act 1934 s. 2(2).
[26] Hafez Abdo, "The Story of the UK Oil and Gas Taxation Policy: History and Trends" (*Oil, Gas & Energy Law*, 4 November 2010), *https://www.ogel.org/article.asp?key=3054* [Accessed 8 September 2022].
[27] Seely, *Taxation of North Sea Oil and Gas* (2022).
[28] Hafez Abdo, "The taxation of UK oil and gas production: Why the windfalls got away" (2010) 38(10) *Energy Policy* 5625.
[29] Hafez Abdo, "Investigating the effectiveness of different forms of mineral resources governance in meeting the objectives of the UK petroleum fiscal regime" (2014) 65(2) *Energy Policy* 48.
[30] Bernard Mommer, *Global Oil and the Nation State* (Oxford: OUP, 2002).
[31] Wood, *UKCS Maximising Recovery Review: Final Report* (2014).
[32] The ring fence prevents taxable profits from oil and gas extraction in the UK and UKCS being reduced by losses from other activities or by excessive interest payments (HMRC, *Oil and Gas Taxation: Transferable Tax History and Retention of Decommissioning Expenditure* (2020)).
[33] NSTA, "Taxation Overview", *https://www.nstauthority.co.uk/exploration-production/taxation/overview/* [Accessed 8 September 2022].
[34] Antony Seely, *Energy (Oil and Gas) Profits Levy Bill 2022–23* (TSO, 2022), Research Briefing, House of Commons Library, *https://researchbriefings.files.parliament.uk/documents/CBP-9578/CBP-9578.pdf* [Accessed 8 September 2022].
[35] HMRC, Internal Manual, *Oil Taxation Manual* (2021).
[36] HMRC, Internal Manual, *Oil Taxation Manual* (2021), "OT00040—The taxation of the UK oil industry: An overview: Legal overview 1918 to Petroleum Act 1998".
[37] *Hansard*, HC Vol 882, cols 459–551 (27 November 1974).

with a safeguard to prevent payments before payback and a generous "oil allowance" which reduced the amount of PRT actually payable by smaller fields. It was ring-fenced on a field-by-field basis and was a deductible charge for calculating income for corporation tax purposes. The rate of PRT was increased to 60 per cent in 1979, then to 70 per cent in 1980, and up to 75 per cent in 1983 before it was abolished for fields that received development consent on or after 16 March 1993. For fields with development consents received prior to 16 March 1993, the rate of PRT was reduced from 75 per cent to 50 per cent in the Finance Act 1993.[38] This action by the Treasury was a response to the reduction in oil and gas prices and increased production costs in the early 1990s and to the cost of PRT repayments to the UK Government—£216 million in 1992–93 (see Table 1, also Charts 1 and 2 below).[39] Furthermore, abolishing PRT for post-1993 fields was, essentially, because such fields were expected to be much smaller, and so much less profitable compared with pre-1993 fields. The "super" tax rate was not thought to be appropriate for the smaller, high-cost and less profitable fields.

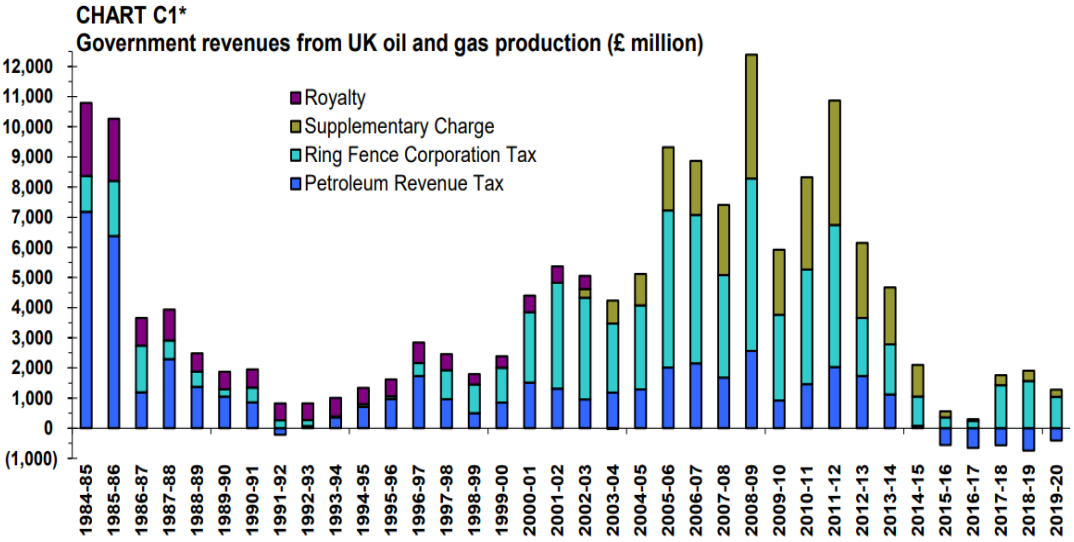
[38] Finance Act 1993 Pt III s.186(1); Abdo, "The Story of the UK Oil and Gas Taxation Policy: History and Trends" (2010).

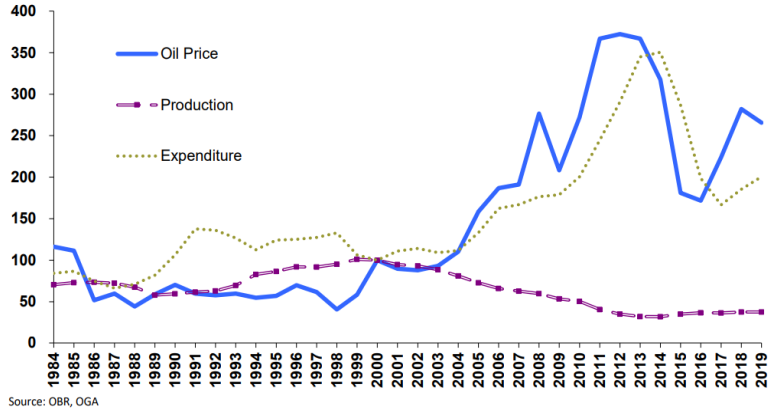
[39] HMRC, *Statistics of Government Revenues from UK Oil and Gas Production* (TSO, 2020), Table 1 and Chart 1, p.9, Chart 2, p.10, *https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/902798/Statistics_of_government_revenues_from_UK_oil_and_gas_production__July_2020_for_publication.pdf* [Accessed 8 September 2022].

Table 1: Government revenues from UK oil and gas production

£ million

Financial Year	Licence Fees	Royalty	Petroleum Revenue Tax (PRT)	Supplementary Petroleum Duty (SPD)	Total CT (corporation tax before ACT set off)	Advance CT (ACT) set-off	Ring fence CT (RFCT)	Supplementary Charge (SC)	Total revenues (excluding gas levy)	Gas Levy (gross)	GDP deflator 2021/22=100
1964/65	2								2		4.922
1965/66	1								1		5.187
1966/67											5.452
1967/68											5.601
1968/69		1							1		5.894
1969/70		2							2		6.300
1970/71	1	3			2		2		6		6.922
1971/72	39	6			4		4		49		7.445
1972/73	4	11			4		4		19		8.077
1973/74	3	12			3		3		18		8.788
1974/75	4	15			5		5		24		10.571
1975/76	2	20			5		5		27		13.161
1976/77	5	71			10		10		86		14.993
1977/78	7	228			10		10		245		17.056
1978/79	9	289	183		93	40	53		574		18.977
1979/80	10	628	1,435		250	78	172		2,323		22.177
1980/81	220	992	2,410		341	97	244		3,963		26.417
1981/82	14	1,396	2,390	2,025	681	270	411		6,506	383	29.199
1982/83	46	1,632	3,274	2,395	521	202	319		7,868	471	31.347
1983/84	19	1,904	6,017		877	430	447		8,817	522	32.844
1984/85	136	2,426	7,177		2,432	1,244	1,188		12,171	500	34.713
1985/86	23	2,057	6,375		2,916	1,085	1,831		11,371	525	36.646
1986/87	21	919	1,188		2,676	1,130	1,546		4,804	515	38.171
1987/88	27	1,024	2,296		1,298	681	617		4,645	502	40.349
1988/89	25	602	1,371		1,195	685	510		3,193	407	43.059
1989/90	33	575	1,050		743	495	248		2,401	335	46.466
1990/91	31	605	860		847	363	484		2,343	291	50.361
1991/92	37	557	-216		638	370	268		1,016	282	53.354
1992/93	34	554	69		682	480	202		1,339	287	54.817
1993/94	43	606	359		258	219	39		1,266	240	56.248
1994/95	41	550	712		380	299	81		1,683	175	57.042
1995/96	49	555	968		766	674	92		2,338	161	58.801
1996/97	48	684	1,729		890	460	430		3,351	198	60.899
1997/98	54	535	963		1,779	821	958		3,331	200	60.642
1998/99	62	343	504		1,605	655	950		2,514		62.027
1999/2000	53	389	853		1,268	120	1,148		2,563		62.379
2000/01	55	552	1,518		2,329		2,329		4,454		63.619
2001/02	59	548	1,310		3,515		3,515		5,432		64.947
2002/03	63	434	958		3,369		3,369	293	5,117		66.323
2003/04	58	-13	1,179		2,291		2,291	766	4,281		68.010
2004/05	56		1,284		2,790		2,790	1,041	5,171		70.029
2005/06	58		2,016		5,210		5,210	2,097	9,381		72.104
2006/07	63		2,155		4,919		4,919	1,790	8,927		74.243
2007/08	57		1,680		3,402		3,402	2,326	7,465		76.318
2008/09	63		2,567		5,716		5,716	4,110	12,456		78.579
2009/10	68		923		2,839		2,839	2,159	5,989		79.814
2010/11	69		1,458		3,810		3,810	3,054	8,391		81.145
2011/12	67		2,032		4,714		4,714	4,126	10,939		82.370
2012/13	69		1,737		1,916		1,916	2,496	6,218		84.031
2013/14	71		1,118		1,665		1,665	1,891	4,745		85.956
2014/15	65		77		970		970	1,056	2,168		86.946
2015/16	71		-562		364		364	196	69		87.486
2016/17	65		-654		245		245	50	-294		89.442
2017/18	62		-569		1,423		1,423	334	1,250		90.982
2018/19	73		-744		1,565		1,565	347	1,241		92.758
2019/20	68		-408		1,080		1,080	194	934		94.865
2020/21	68		-250		422		422	76	316		100.221





* Chart C1 shows the annual tax yield and its separate components since 1984-85. Chart C2 shows three of the main determinants of tax liability: annual production, the sterling oil price and total expenditure. Each is shown as an index based on 2000 = 100.

In the face of the drop in oil prices in 2014 and the UK objective of enhancing investments and Maximising Economic Recovery from the UKCS,[40] the rate of PRT was reduced to 35 per cent for chargeable periods ending 31 December 2015, with effect from 1 January 2016,[41] but this was short lived as the rate was reduced to 0 per cent in the March Budget of 2016 (and later Finance Act 2016

[40] HMRC, *Policy Paper—Oil and Gas Taxation: Reduction in Petroleum Revenue Tax and Supplementary Charge* (TSO, 2016), *https://www.gov.uk/government/publications/oil-and-gas-taxation-reduction-in-petroleum-revenue-tax-and-supplementary-charge* [Accessed 8 September 2022].
[41] Finance Act 2015 s.52.

(FA 2016))[42] so the 35 per cent rate was never, in practice, in effect. Rationales for these changes were the reduced oil prices, and reduced production from, and investments in, the UKCS. Therefore, in order to reduce uncertainty, enhance investments and maintain energy security, the UK Government felt that a tax reform was necessary to increase the attractiveness of investments in the UKCS.[43] Bringing PRT down to 0 per cent, rather than abolishing it, was to allow companies to claim their decommissioning tax relief and allowable losses against historical PRT payments.[44]

(b) Ring fence corporation tax (RFCT)

Oil and gas companies operating on the UKCS are subject to corporation tax ring-fenced at the company level at a rate of 30 per cent (the normal corporation tax rate is currently 19 per cent). The RFCT is calculated in the same way as corporation tax apart from the ring fence basis which treats oil and gas activities as separate trades. "The ring fence prevents taxable profits from oil and gas extraction being reduced by losses from other activities or by excessive interest payments".[45] The ring-fenced oil and gas profits benefit from allowances that are not available under the general corporation tax regime, for example, the 100 per cent first year capital allowance and the extended loss carry-back on decommissioning costs of oil and gas installations.[46] The rate of RFCT was 52 per cent (1964–93), but was reduced to 50 per cent in 1984, to 45 per cent in 1985, and then to 40 per cent in 1986, and stayed at 35 per cent during the period 1987–90 before it was decreased to 34 per cent in 1991 and to 33 per cent during the period 1992–96. It was then reduced again to 32 per cent in 1997–98 before it settled at 30 per cent in 1999, since when it has not changed.

(c) Supplementary charge (SC)

Enhancements of oil and gas companies' profits in the early 2000s stimulated the UK Government in 2002 to introduce, in the Finance Act 2002, a supplementary charge (SC) at the rate of 10 per cent on oil and gas companies' profits from the UK and UKCS.[47] This was also in line with the UK Government's key objective of delivering a tax regime that promoted long-term investment while securing a fair return to the British people from their oil and gas resources. Supplementary charge is ring-fenced with no deductions for finance costs. The rate of SC has been subject to a number of amendments since 2002, having been increased to 20 per cent by the Finance Act 2006, then to 32 per cent by the Finance Act 2011, and then reduced to 20 per cent by the Finance Act 2015 and to 10 per cent by the FA 2016. Changes in SC rates were underpinned by fluctuations in oil and gas prices, production, investments, and profits made by the oil and gas industry.

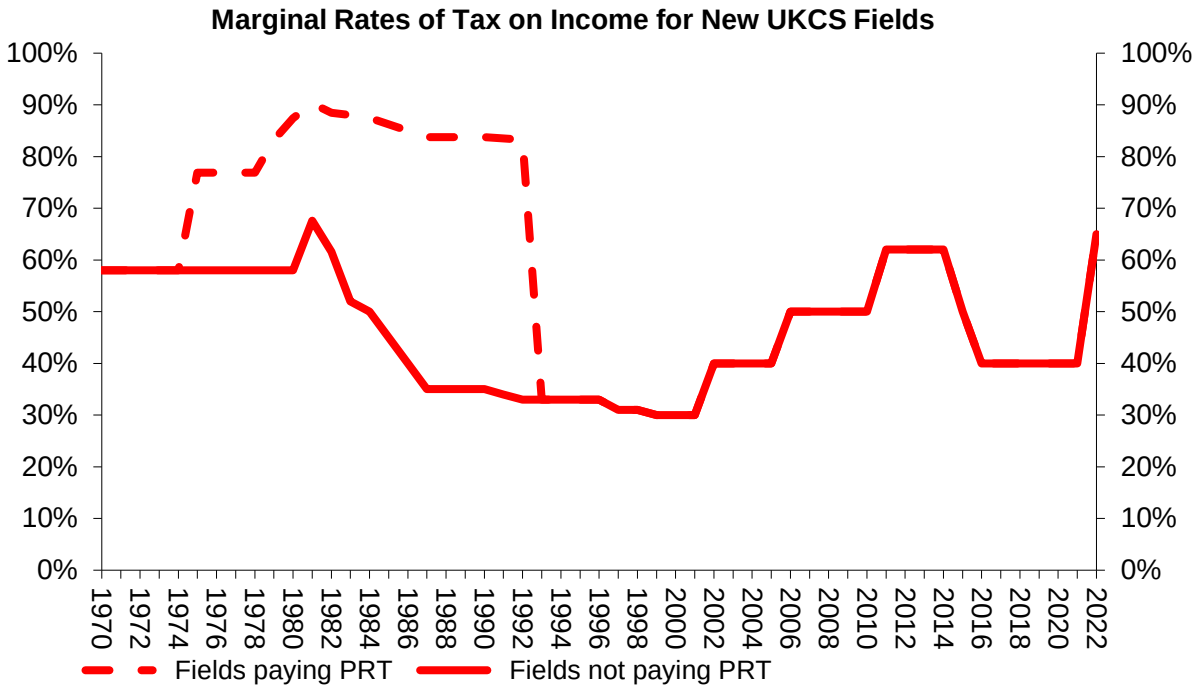
(d) Energy profits levy (EPL)

With effect from 26 May 2022, the UK Government introduced an EPL: "a temporary additional charge on a company's ring fence profits"[48] at a rate of 25 per cent on profits generated by oil and gas

[42] Finance Act 2016 s.140.
[43] HMRC, *Oil and Gas Taxation: Reduction in Petroleum Revenue Tax and Supplementary Charge* (2016).
[44] CW Energy, "Budget update—consequences of the PRT zero rate" (2016), *https://cwenergy.co.uk/tag/prt-zero-rate/* [Accessed 8 September 2022]; NSTA, "Taxation Overview" (2022).
[45] HMRC, *Oil and Gas: Ring Fence Corporation Tax* (TSO, 2015), *https://www.gov.uk/guidance/oil-gas-and-mining-ring-fence-corporation-tax* [Accessed 8 September 2022].
[46] PwC, *United Kingdom—Corporate: Taxes on Corporate Income* (27 July 2022), *https://taxsummaries.pwc.com/united-kingdom/corporate/taxes-on-corporate-income* [Accessed 8 September 2022].
[47] HMRC, *Oil and Gas Taxation: Reduction in Petroleum Revenue Tax and Supplementary Charge* (2016).
[48] NSTA, "Taxation Overview" (2022).

companies in the UK. This increases the petroleum marginal tax rate to 65 per cent.[49] What is noticeable about the EPL is that decommissioning costs are not deductible against this levy.[50] Figure 1[51] presents the historical changes in the UK petroleum marginal tax rate.

Figure 1



The ring-fence element of the UK petroleum taxation regime reduces the possibility of tax avoidance by setting losses from other investment activities, such as refining or transportation, against profits made from the upstream investments. One of the complex features of the system, however, is that new taxes have always been introduced with additional allowances and reliefs, or additional allowances and reliefs have been introduced subsequently. Although this may be an attempt to increase the fairness of the tax system, it adds also to its complexity. For example, the decommissioning costs of oil and gas assets are classified as removal costs under International Accounting Standard (IAS) 16—*Property, Plant and Equipment*.[52] Therefore, depreciating the decommissioning cost element of an oil and gas asset is similar to depreciating other tangible assets of oil and gas companies and is part of the allowable costs (in the form of capital allowances) for tax calculations. Consequently, excluding decommissioning costs from allowable deductions against RFCT before April 2002 and against EPL, and restricting the relief against SC to 20 per cent[53] raises questions about the fairness of the UK petroleum fiscal regime (the SC rate was 32 per cent between 2011 and 2015). However, since the UK petroleum fiscal regime

[49] HM Treasury, *Policy Paper—Energy Profits Levy Factsheet* (TSO, 2022), *https://www.gov.uk/government/publications/cost-of-living-support/energy-profits-levy-factsheet-26-may-2022* [Accessed 8 September 2022).

[50] Claire Angell, "Draft legislation published for the Energy Profits Levy" (*KPMG*, 27 June 2022), *https://home.kpmg/uk/en/home/insights/2022/06/tmd-draft-legislation-published-for-the-energy-profits-levy.html* [Accessed 8 September 2022).

[51] Made available from the NSTA via direct, personal communication to the authors.

[52] International Financial Reporting Standards Foundation, *IAS 16 Property, Plant and Equipment* (London: IFRS Foundation, 2022). The text of IAS 16 is available at *https://www.ifrs.org/issued-standards/list-of-standards/ias-16-property-plant-and-equipment/* [Accessed 8 September 2022].

[53] Finance Act 2012 Sch.21.

is not constructed to capture a share of economic rent when oil and/or gas prices increase, it is only fair to increase rates of existing taxes and/or introduce new taxes that allow the capture of a fair slice of augmented profits when any increases are made by oil and gas companies. The same argument applies when oil and gas prices decline. This mechanism of introducing new taxes, increasing or decreasing rates of existing taxes, or even abolishing taxes and duties, underpins the changes in the tax marginal rate shown in Figure 1.

(3) Current issues in the oil and gas sector

(a) Decommissioning UKCS oil and gas assets in context

Oil and gas companies operating in the UK are obliged by national and international laws (for example, UNCLoS 1982, the 1992 Convention for the Protection of the Marine Environment of the North East Atlantic (known as the Oslo and Paris (OSPAR) Conventions), and the Petroleum Act 1998) to remove any installations at the end of their economic lives from a given field or area.[54] Decommissioning oil and gas installations is expensive, challenging and the beginning of a costly operation for oil and gas companies when production has ceased.[55]

The latest report from the UK OGA shows that 7,800 wells have been drilled on the UKCS, of which 2,128 are active.[56] These wells are located in 300 oil and gas fields across the UKCS.[57] The NSTA estimation of the cost of decommissioning installations and pipelines on the UKCS between 2018 and 2055–56 was £49 billion, of which £24 billion is the UK Government share in terms of decommissioning tax relief. However, these sums have been recently amended to an estimate of £44.5 billion for decommissioning costs, although it is less clear what would be the Government's share.[58] Notwithstanding, it is crucial to establish whether this share is a contribution by the UK Government towards the decommissioning costs of the oil and gas industry or a tax rebate.

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[54] Davar and Shirazi, "Decommissioning in the UK Continental Shelf: A litigator's perspective" [2015] I.E.L.R. 192; Department for Business, Energy and Industrial Strategy, *Guidance Notes—Decommissioning of Offshore Oil and Gas Installations and Pipelines* (TSO, 2018), *https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/760560/Decom_Guidance_Notes_November_2018.pdf* [Accessed 8 September 2022]; Offshore Petroleum Regulator for Environment & Decommissioning, *Decommissioning of Offshore (Oil and Gas) Installations and Pipelines*: *Guidance on charging a fee in respect of offshore (oil and gas) installations and pipelines decommissioning programmes under the Petroleum Act 1998*, *https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/655916/Guidance_-_charging_a_fee_for_offshore__oil_and_gas__installtions_and_pipelines_under_the_Petroleum_Act_1998.pdf* [Accessed 8 September 2022]; HM Treasury, *Tax Issues for Late-Life Oil and Gas Assets: Discussion Paper* (TSO, 2017), *https://www.gov.uk/government/consultations/tax-issues-for-late-life-oil-and-gas-assets* [Accessed 8 September 2022].

[55] Mark Kaiser, "Accounting for offshore structure retirement obligations: Process and factor description" (2005) 24(3) *Petroleum Accounting and Financial Management Journal* 64.

[56] OGA, *Wells Insight Report* (TSO, 2018), *https://www.ogauthority.co.uk/media/5107/oga_wells_insight_report_2018.pdf* [Accessed 8 September 2022].

[57] Wood, *UKCS Maximising Recovery Review: Final Report* (2014). On the UKCS, "[t]here are over 320 fixed installations, 250 subsea systems, 20,000 km of pipelines and approximately 7,800 wells in the UKCS" which require decommissioning—see OGA *Decommissioning Strategy* (TSO, 2021), p.5, *https://www.nstauthority.co.uk/media/7538/decommissioning-strategy-may-2021.pdf* [Accessed 8 September 2022].

[58] NSTA, *Estimates of the Remaining Exchequer Cost of Decommissioning UK Upstream Oil and Gas Infrastructure (August 2019)* (TSO, 2019), *https://www.nstauthority.co.uk/media/5960/exchequer_cost_decommissioning_august_2019.pdf* [Accessed 8 September 2022]; and more recently, *https://www.nstauthority.co.uk/media/8321/decom_cost-estimate-2022_020822_final_v3.pdf* [Accessed 8 September 2022].

(b) Decommissioning tax relief

Realising the financial impact of decommissioning costs on companies' financial statements, the UK Government introduced a tax relief for decommissioning costs in the CAA 2001.[59] This relief is at rates based on tax previously paid on hydrocarbon production from a field (PRT, SC or RFCT). This is known as "tax history" or "tax capacity".[60] The relief is principally limited to the tax that the company has paid in respect of certain fields. In the case of RFCT and SC, as these charges are ring-fenced at a company level, decommissioning costs can be relieved as follows: (1) by being carried forward against future taxable ring-fenced profits; (2) by surrender to other group companies in the same year (as group relief); or (3) by being carried back against previous years' ring-fenced taxable profits on a last in-first out basis, up to April 2002.[61] (In the case of PRT, any losses from decommissioning can be carried back against taxable profits of the same field in previous years on a last in-first out basis without a limit. Refundable PRT[62] is paid with interest and is subject to RFCT and SC adjustments.) The extended losses' carry-back disincentivises operators from decommissioning profitable fields early. It is key to mention that since decommissioning costs are not allowable deductions for EPL, this levy is not part of an operator's tax history.[63]

Initially, the relief allowed losses attributable to qualifying decommissioning expenditure to be carried back against past profits for a maximum of three years. However, in 2008 the carry-back period was extended so that losses could be set against profits generated from 17 April 2002. The rationale for this extension was to ensure that tax recovery was not a contributing factor in bringing forward the decommissioning of mature fields during the final years of production, and to allow companies to recover their decommissioning tax relief from a reasonably fit tax portfolio. In fact, this tax adjustment aligns with the objective of the UK NSTA of Maximising Economic Recovery from oil and gas fields within the UKCS[64] and thus enhances the energy security of the UK.[65] Introducing the EPL contradicts this objective as it does not exclude marginal and less profitable fields, thereby reducing the return from these fields and possibly leading to their early closure. Therefore, this levy adds to the complexity and uncertainty of the UK petroleum fiscal regime, and consequently disincentivises investments in the UKCS.[66] Moreover, a critical condition for the decommissioning tax relief set by the FA 2019 is as

[59] Capital Allowances Act 2001 ss.162–165.

[60] HM Treasury, *Tax Issues for Late-Life Oil and Gas Assets: Discussion Paper* (2017).

[61] HM Treasury, *Tax Issues for Late-Life Oil and Gas Assets: Discussion Paper* (2017).

[62] "For PRT purposes, an asset transfer itself has no effect, and the PRT losses and unclaimed expenditure transfer with the field. Any PRT refund from losses that are generated by the new owner and carried back to the time of the seller's ownership will be repaid to the seller. (The seller will be subject to RFCT and SC on any such refund). Sale and purchase agreements will normally provide that the seller must pay forward the refund (after RFCT and SC) to the buyer. This has the effect that the tax history is effectively transferred for PRT purposes" (HM Treasury, *Tax Issues for Late-Life Oil and Gas Assets: Discussion Paper* (2017), p.14).

[63] HM Treasury, *Policy Paper—Energy Profits Levy—Technical Note* (TSO, 2022), *https://www.gov.uk/government/publications/cost-of-living-support/energy-profits-levy-technical-note* [Accessed 8 September 2022].

[64] OGA, *The Maximising Economic Recovery Strategy for the UK* (TSO, 2015), *https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/509000/MER_UK_Strategy_FINAL.pdf* [Accessed 8 September 2022].

[65] UK decommissioning policy and practices are centred around the need to maximise energy production as a contribution to UK energy security, and to take impacts on climate change into account (Department of Energy and Climate Change, *Decommissioning of Offshore Oil and Gas Installations and Pipelines under the Petroleum Act 1998 URN 09D/734* (TSO, 2011), p.2; Department of Energy and Climate Change, *Energy Security Strategy* (TSO, 2012), *https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/65643/7101-energy-security-strategy.pdf* [Accessed 8 September 2022]).

[66] Andrew Terry, "UK Government announced Energy Profits Levy—windfall tax on oil and gas companies" (*Keystone Law*, 6 June 2022), *https://www.keystonelaw.com/keynotes/uk-government-announced-energy-profits-levy-windfall-tax-on-oil-and-gas-companies* [Accessed 8 September 2022]; EY, "UK announces new 25% energy profits levy" (26 May 2022), *https://www.ey.com/en_gl/tax-alerts/uk-announces-new-25--energy-profits-levy* [Accessed 8 September 2022].

follows: "[A]t the end of a post-acquisition accounting period of the purchaser, the total decommissioning expenditure amount exceeds the total net profits amount".[67]

This condition is controversial, as, in order to qualify for decommissioning tax relief, an operator must experience loss. This condition lacks clarity and may open the door to continuous and complicated debate among stakeholders. It is particularly relevant in cases where companies may want to decommission part of an operating field that is a profit-making asset, which means such an operator would not be allowed to claim decommissioning tax relief for the decommissioned assets.

Another issue that might complicate the sale of late-life assets is the "valuation gap". This is the difference in the value of the decommissioning tax relief on a given field as perceived by the seller and the buyer respectively, with the buyer often perceiving the value to be lower. Similarly, the issue of a "no clean break" might also complicate the sale of late-life assets. In accordance with the UK Government's desire to ensure that the UK taxpayer is not exposed to the risk of default in meeting the costs associated with decommissioning,[68] section 29 of the Petroleum Act 1998 requires that oil and gas licence holders be jointly and severally liable for the decommissioning costs of a field when it is due for decommissioning.[69] In order to reduce uncertainty about their liabilities, sellers require securities, assurances or guarantees to be provided by the buyer, for example, in the form of letters of credit, which are referred to as decommissioning security notes/letters. Banks provide these letters, at a cost, but banks and finance providers generally are increasingly reluctant to become involved in the fossil fuel business given the fluctuations of oil and gas prices, "net zero" legislation and the climate change regulations that are likely to lead to impairments of oil and gas assets and stranding of oil and gas reserves and therefore financial losses for oil and gas companies,[70] low oil prices and the move towards sustainable energy.[71] Such assurances are costly and increase the burden and costs of decommissioning for the buyer. As one leading authority comments:

> "Sellers have sought to ensure a clean break and to insulate themselves against the risk of being made liable for the ultimate costs of decommissioning by seeking security for the estimated costs of decommissioning from buyers. Co-venturers, faced with new

[67] Finance Act 2019 Sch.15 Pt 5 para.30(1)(b).

[68] Judith Aldersey-Williams, "Decommissioning security" in Nicholas Antonas and Marc Hammerson (eds), *Oil and Gas Decommissioning: Law, Policy, and Comparative Practice*, 2nd edn (Surrey: Global Law and Business Ltd, 2016); Department of Energy and Climate Change, *Decommissioning of Offshore Oil and Gas Installations and Pipelines under the Petroleum Act 1998 URN 09D/734* (2011); Department of Energy and Climate Change *Energy Security Strategy* (2012); HM Treasury, *Tax Issues for Late-Life Oil and Gas Assets: Discussion Paper* (2017).

[69] See also Department of Energy and Climate Change *Decommissioning of Offshore Oil and Gas Installations and Pipelines under the Petroleum Act 1998 URN 09D/734* (2011); House of Commons, Committee of Public Accounts, *Minimising Costs and Maximising Benefits of Decommissioning to the Taxpayer* (TSO, 2019), *https://publications.parliament.uk/pa/cm201719/cmselect/cmpubacc/1742/174206.htm* [Accessed 8 September 2022].

[70] Ben Caldecott and Jeremy McDaniels, *Stranded generation assets: Implications for European capacity mechanisms, energy markets and climate policy* (Oxford: Smith School of Enterprise and the Environment, University of Oxford, 2014), *https://www.smithschool.ox.ac.uk/research/sustainable-finance/publications/Stranded-Generation-Assets.pdf* [Accessed 8 September 2022]; Ben Caldecott, James Tilbury and Yuge Ma, *Stranded Down Under? Environment Related Factors Changing China's Demand for Coal and What this Means for Australian Coal Assets* (Oxford: Smith School of Enterprise and the Environment, University of Oxford, 2013), *https://ora.ox.ac.uk/objects/uuid:27d52eb8-0c8b-44a6-b395-31c660e32855* [Accessed 8 September 2021]; Jean-Francois Mercure et al, "Macroeconomic impact of stranded fossil fuel assets" (2018) 8 *Nature Climate Change* 588.

[71] J. Reid, "Decommissioning reform in UKCS" in Antonas and Hammerson (eds), *Oil and Gas Decommissioning: Law, Policy, and Comparative Practice* (2016), p.67; Aldersey-Williams, "Decommissioning security" in Antonas and Hammerson (eds), *Oil and Gas Decommissioning: Law, Policy, and Comparative Practice* (2016), p.87; Gordon, Paterson and Vass, "The Wood Review and Maximising Economic Recovery upon the UKCS" in Gordon, Paterson and Üşenmez (eds), *UK Oil and Gas Law: Current Practice and Emerging Trends: Vol.I: Resource Management and Regulatory Law* (2018).

> partners who lack the financial muscle of traditional players, have sought similar protection against the threat of joint and several liability for decommissioning. Security has been provided largely in the form of letters of credit, requiring both an annual fee and, for many companies, the provision of collateral to the issuing bank, or, where collateral is not available, a commensurate reduction in their borrowing base. This requirement has been a significant barrier to moving assets into the right hands—particularly to smaller, leaner companies able and willing to exploit these late-life assets."[72]

Formal decommissioning security agreements often exist, which are commercial agreements established to ensure the availability of funds when the time comes to decommission an asset. These agreements may be entered into between existing licensees, or between current and past licensees.[73] In addition, to increase investors' confidence, provide certainty in relation to the decommissioning tax relief that investors will receive and address the cost of security, the UK Government introduced, in section 80 of the Finance Act 2013, the decommissioning relief deed, which is a contract between the UK Government and an operator on the UKCS. The decommissioning relief deed provides that, in such circumstances as are specified in the agreement, if the amount of tax relief in respect of any decommissioning expenditure incurred by the company is less than an amount determined in accordance with the agreement (the reference amount), the difference is payable to the company.[74] The decommissioning relief deed aims

> "to encourage investment by existing owners of assets, increase asset trades and free up capital currently put aside to provide security, thereby extending the productive life of many fields—all at no cost to the Exchequer".[75]

The introduction of the decommissioning relief deed with the assurance of tax relief on decommissioning expenditure, has "allowed buyers to move away from provision of security on a 'pre-tax' to a 'post-tax' basis, reducing security required by between 50% and 75%".[76]

A recent and significant development in respect of decommissioning tax relief has been the argument brought to the High Court by three climate activists for a judicial review "over whether UK's tax breaks for the oil and gas sector represent unfair subsidies for the fossil fuel industry".[77] The campaigners argued (unsuccessfully) that the UK Government's oil and gas strategy conferred an unfair

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[72] CMS Law-Now, "Decommissioning campaign—issues with late life asset transfers" (15 February 2017), *https://www.cms-lawnow.com/ealerts/2017/02/decommissioning-campaign--issues-with-late-life-asset-transfers?cc_lang=en* [Accessed 8 September 2022].

[73] HM Treasury, *Decommissioning Relief Deeds: Summary of Responses* (TSO, 2012), *https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/190266/consult_responses_decommissioning_relief_deeds_111112.pdf* [Accessed 8 September 2022].

[74] HM Treasury, *Decommissioning Relief Deed—Claim Statement* (TSO, 2016), *https://www.gov.uk/government/publications/decommissioning-relief-deeds-claim-statement* [Accessed 8 September 2022]. See also HM Treasury, *Decommissioning Relief Deeds: Increasing Tax Certainty for Oil and Gas Investment in the UK Continental Shelf* (TSO, 2012), *https://www.gov.uk/government/consultations/decommissioning-relief-deeds-increasing-tax-certainty-for-oil-and-gas-investment-in-the-uk-continental-shelf* [Accessed 8 September 2022].

[75] CMS Law-Now, "Decommissioning Relief Deeds—a world first!" (8 November 2013), *https://www.cms-lawnow.com/ealerts/2013/11/decommissioning-relief-deeds-a-world-first?cc_lang=en* [Accessed 8 September 2022].

[76] CMS Law-Now, "Innovation: Making deals happen in North Sea Oil and Gas M&A" (8 March 2017), *https://www.cms-lawnow.com/publications/2017/03/innovation-making-deals-happen-in-north-sea-oil-and-gas-ma?cc_lang=en&ec_as=3DEE3B90FBEB4E65A485F2CE26D41EB7* [Accessed 8 September 2022].

[77] Scarlett White, "High Court throws out oil and gas case", *Accountancy Daily*, 18 January 2022, *https://www.accountancydaily.co/high-court-throws-out-oil-and-gas-tax-case* (subscriber only access) [Accessed 8 September 2022]; Scarlett Evans, "UK High Court rejects legal challenge to North Sea oil and gas" (*Offshore Technology*, 18 January 2022), *https://www.offshore-technology.com/news/uk-high-court-rejects-legal-challenge-to-north-sea-oil-and-gas/* [Accessed 8 September 2022]. The case referred to is *R. (on the application of Cox) v Oil And Gas Authority* [2022] EWHC 75 (Admin) (18 January 2022).

advantage on multinationals that had developed offshore resources, and undercut the meaning of Maximising Economic Recovery as it ignored the tax breaks to drilling companies. However, the judge decided that what "maximum economic recovery means is up to the Oil and Gas Authority, and not the Court, and the definition does not require consideration of tax flows".

(c) Transfer of late-life oil and gas assets

Transferring late-life assets from larger to smaller operators, while encouraged by the UK Government, has been received with caution.[78] This is because of the concern felt that such smaller operators might not be financially and technically able to undertake the required decommissioning operations and that this might result in the UK Government becoming liable for the decommissioning costs of fields operated by these companies.[79] This was the reason for the introduction of the "no clean break" obligation, as indicated above. Furthermore, and as a security measure, the UK Government has in some cases requested oil and gas operators to set aside financial reserves to meet future decommissioning obligations to ensure that the financial bill does not fall on taxpayers.[80]

The UK Government has realised the difficulties that have faced the transfer of late-life oil and gas assets between operators on the UKCS,[81] and thus the obstacles to Maximising Economic Recovery from these assets. Therefore, FA 2019 introduced legislation to allow the transferability of tax history between operators on the UKCS. According to HMRC:

> "TTH [transferability of tax history] will be available for licence transfers that receive Oil and Gas Authority (OGA) approval on or after 1 November 2018."[82]

The rationale for this reform was put forward by the Government as follows:

> "The government's objective is to maximise economic recovery of its remaining oil and gas reserves, while ensuring the nation receives a fair return on its hydrocarbon resources."[83]
>
> "Extending the productive lives of late-life oil and gas fields is an important aspect of this objective, as it leads to new investment, delaying decommissioning and supporting activity in the UKCS for longer."[84]

However, despite being expected to help in facilitating the transfer of assets between operators,[85] the transferability of tax history legislation included a number of rules and restrictions on the transfer of tax history between sellers and buyers. For instance, the transferable tax history applies only to RFCT

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[78] Aldersey-Williams, "Decommissioning security" in Antonas and Hammerson (eds), *Oil and Gas Decommissioning: Law, Policy, and Comparative Practice* (2016), p.87; Gordon, Paterson and Vass, "The Wood Review and Maximising Economic Recovery upon the UKCS" in Gordon, Paterson and Üşenmez (eds), *UK Oil and Gas Law: Current Practice and Emerging Trends: Vol.I: Resource Management and Regulatory Law* (2018).
[79] House of Commons, Committee of Public Accounts, *Minimising Costs and Maximising Benefits of Decommissioning to the Taxpayer* (2019).
[80] House of Commons, Committee of Public Accounts, *Minimising Costs and Maximising Benefits of Decommissioning to the Taxpayer* (2019).
[81] Claire Angell, "Finance Act 2019: Transferable Tax History in the UK North Sea" (*KPMG*, 2019), *https://home.kpmg/uk/en/home/media/press-releases/2021/03/uk-governments-north-sea-transition-deal.html* [Accessed 30 August 2022].
[82] HMRC, *Oil and Gas Taxation: Transferable Tax History and Retention of Decommissioning Expenditure* (2020), under "General description of the measure".
[83] HM Treasury, *An Outline of Transferable Tax History* (TSO, 2017), *https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/660596/An_outline_of_Transferable_Tax_History_web.pdf* [Accessed 8 September 2022].
[84] HMRC, *Oil and Gas Taxation: Transferable Tax History and Retention of Decommissioning Expenditure* (2018), under "Policy objective".
[85] HMRC, *Oil and Gas Taxation: Transferable Tax History and Retention of Decommissioning Expenditure* (2018).

and SC, but not to PRT; the amount of tax history transferred cannot be subsequently adjusted; transferability of tax history from seller to buyer will take place on a last-in-first-out basis; any transferred tax history would be capped at an estimate of the buyer's share of the decommissioning cost in the decommissioning security agreement; an independent third party will be used to verify the decommissioning estimate; and once the transfer has taken place, the tax history transferred to the buyer will no longer be available to the seller.

(d) Fairness of the UK petroleum taxation system

The UK petroleum fiscal regime does not allow tax deductions for provisions for decommissioning costs or for depreciation of these costs over the economic lives of fields, so while accounting provisions for decommissioning costs may be made, they are not tax deductible. Decommissioning expenditure is tax deductible only when actually incurred, as indicated above (although not, as noted as regards the 25 per cent EPL).[86] Therefore, by the time of decommissioning an oil and/or gas asset, oil companies would have overpaid tax on their overall profit from the decommissioned field(s). Oil companies are entitled to claim back, via decommissioning tax relief, part of the overpaid tax after they decommission their assets and incur the cash costs.[87] Companies' claims can be based on the amount of RFCT and SC they have paid since April 2002 and the PRT they have paid in total. As noted earlier, this is referred to as "tax history". The issue of limiting the tax history of the RFCT and SC to the period since April 2002 raises a concern about the fairness of UK petroleum taxation, in that operators are not entitled to a repayment of tax paid before April 2002. Furthermore, excluding the EPL from the tax history puts extra pressure on oil and gas companies, particularly the smaller and less profitable ones, which may be an obstacle to the transfer of late-life-assets, should this levy not be removed in 2025, as planned at the time of its introduction.[88] Moreover, the fact of having to wait till after a field is decommissioned before being able to claim part of the overpaid tax via decommissioning tax relief is another issue that raises concern about the fairness of the UK petroleum taxation system. The claiming of decommissioning tax relief does not grant companies immediate repayments, as they then have to wait for sometimes almost two years before being repaid the overpaid tax to which they are entitled. In addition, the issue of a tax refund has been interpreted by some as a cash contribution by the UK Government, thus making decommissioning of late-life oil and gas assets relevant to the general public who wants to make sure that public money is not spent on decommissioning oil and gas assets.[89]

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[86] William Arrenberg and Isaak Zailer, "UK Tax and North Sea decommissioning" (2012) 23(4) *International Tax Review* 74, *https://heinonline.org/HOL/LandingPage?handle=hein.journals/intaxr23&div=98&id=&page=* [Accessed 8 September 2022]; HMRC, Internal Manual, *Business Income Manual* (22 November 2013, updated 7 March 2022), BIM46510, "Specific Deductions: Provisions: Allowability for Tax", *https://www.hmrc.gov.uk/manuals/bimmanual/bim46510.htm* [Accessed 8 September 2022]; Derek Leith, "Are there any tax levers left to pull for the UK oil and gas industry?" (*Energy Voice*, 14 May 2020), *https://www.energyvoice.com/opinion/240642/are-there-any-tax-levers-left-to-pull-for-the-uk-oil-and-gas-industry/* [Accessed 8 September 2022].

[87] Derek Leith, "North Sea decomm tax relief broken down" (*Energy Voice*, 13 March 2017), *https://www.energyvoice.com/opinion/133846/eys-derek-leith-north-sea-decomm-tax-relief-broken* [Accessed 8 September 2022].

[88] OEUK, press release, *Windfall taxes risk lasting damage to the UK's offshore sector and energy security, warns Offshore Energies UK* (25 May 2022), *https://oeuk.org.uk/windfall-taxes-risk-lasting-damage-to-the-uks-offshore-sector-and-energy-security-warns-offshore-energies-uk/* [Accessed on 26 August 2022]. EY, "UK announces new 25% energy profits levy" (2022).

[89] Paul Ekins, Robin Vanner and James Firebrace, *Decommissioning of Offshore Oil and Gas Facilities: Decommissioning Scenarios—A Comparative Assessment Using Flow Analysis* (London: Policy Studies Institute, 2005), *https://d1wqtxts1xzle7.cloudfront.net/50778458/Decommissioning-Working_paper-with-cover-page-v2.pdf?Expires=1661871373&Signature=YGkmhfZ15o1okFDJRIuuAQy-Qx1hmK~BdqoMnPo1MxVEJBWA0RN6gari00GYMsWiSzL39uPjWAm4h2-yEx5dRYjwe~XgFhVf22SAH-4ikazdhF8-eAudRBzH20Rn-YnSeNV0HPZjt6hlicRaNsilfNlXNX-hzIPWAAGhwXz8~I4MhySYDJFZEK55QkqmpeDEWkpA5P~Lb3sD90CfJqBoh0dIS6HQwHCWpfiHlsqh4f9Ujs*

(e) Extending the lives of UKCS late-life assets

The rising costs of oil and gas exploration and production and the lack of access to infrastructure, coupled with the fluctuations in oil prices, "net zero" and other climate change regulations, the lack of a skilled workforce, and the instability of the UK petroleum fiscal regime,[90] make investments in the UK North Sea oil fields significantly challenging.[91] Whilst these issues enhance the likelihood of decommissioning, sustained efficiency improvements and cost reduction could defer cessation of production and therefore push decommissioning further into the future.[92] Smaller and marginal sites are better operated by smaller and more specialised companies which, owing to their lower overhead costs and greater specialisation in this niche area of investment, are able both to obtain a reasonable return for themselves and extract the remaining oil and gas resources thus maximising economic recovery from small and marginal fields.[93]

Owing to the maturity of UKCS oil and gas fields, the major oil and gas operators may prefer to shift investments into more profitable areas or to other investment opportunities. To do so, old marginal and non-profitable fields would have to be either abandoned and decommissioned or sold to smaller, but more cost effective, operators. The first option does not seem to be practicable in so far as remaining petroleum resources can be extracted from these fields.[94] The second option which requires transferring ownership of these late-life assets between operators seems to be preferred by the UK Government as it extends the economic lives of these assets, maximises economic recovery and provides a source of domestic energy.[95] In theory, this would aid the country's energy security,[96] support jobs,[97] and make available financial resources and hard currencies for the UK Government to use.[98] From a seller's point of view, transferring late-life assets could unlock the equivalent of decommissioning tax relief via the sale price of the asset: such relief could be lost should the operator not make losses in the year when decommissioning the asset. However, the seller may fear that the financial capability of a buyer may not allow for the decommissioning of the asset when due. In accordance with section 29 of the Petroleum Act 1998, the decommissioning liability may, therefore, fall back on to the seller who would have lost access to the tax history if this was transferred to the buyer in the deal. Therefore, as a security measure, the seller may opt to transfer the asset to the buyer, but keep the decommissioning liability, and thus not transfer the tax history to the buyer.

However, from a buyer's perspective, the transfer of late-life assets is feasible provided appropriate returns are achievable and outweigh expenses, including decommissioning costs. Therefore, in order to benefit from decommissioning tax relief, a buyer needs also to benefit from the transferability

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[90] Jessica Brewer, "What obstacles do North Sea operators face on the path to net zero? Oil and gas players must evolve to retain a licence to operate" (*Wood Mackenzie*, 2021), *https://www.woodmac.com/news/opinion/north-sea-upstream-at-the-forefront-of-the-energy-transition/* [Accessed 8 September 2022].

[91] HM Treasury, *Review of the Oil and Gas Fiscal Regime: call for evidence* (TSO, 2014), *https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/336699/oil_and_gas_fiscal_review_call_for_evidence.pdf* [Accessed 8 September 2022].

[92] Wood, *UKCS Maximising Recovery Review: Final Report* (2014); Oil & Gas UK, *Decommissioning Insight 2016* (2016).

[93] Parente et al, "Offshore decommissioning issues: Deductibility and transferability" (2006) 34(15) *Energy Policy* 1992.

[94] OGA, *The Maximising Economic Recovery Strategy for the UK* (2015).

[95] Oil & Gas UK, *Decommissioning Insight 2016* (2016).

[96] Department of Energy and Climate Change, *Energy Security Strategy* (2012); Gordon, Paterson and Vass, "The Wood Review and Maximising Economic Recovery upon the UKCS" in Gordon, Paterson and Üşenmez (eds), *UK Oil and Gas Law: Current Practice and Emerging Trends: Vol.I: Resource Management and Regulatory Law* (2018).

[97] Wood, *UKCS Maximising Recovery Review: Final Report* (2014).

[98] Parente et al, "Offshore decommissioning issues: Deductibility and transferability" (2006) 34(15) *Energy Policy* 1992.

of tax history from the seller in addition to transferring the asset's ownership. However, the extent to which the transfer of tax history enhances the transferability of ownership of late-life-assets is a practical question. Since transferability of tax history between operators aims to enhance the transferability of oil and gas assets and sustain production and energy security for the nation, the policy should guarantee to the buyer, who could be a small operator, economic returns that are sufficient to enhance the buyer's cash flow and profits. Introducing new taxes, such as the EPL, adds therefore to investment costs and reduces profits, and so may contradict the aim of transferring ownership of late-life assets between operators and bring forward the decommissioning of such assets instead.

(4) Research design and methods

Owing to the lack of academic literature on this topic, this article is exploratory and explanatory in nature. The authors have utilised a qualitative approach in the conduct of their research. The analysis of governmental, non-governmental and industry documents in sections 2 and 3 indicated the issues arising and gave rise to the specific research questions identified in section 1, forming a basis for semi-structured interviews. These interviews were then used to explore the impacts of the current UK petroleum fiscal regime on transfer of ownership of late-life oil and gas assets on the UKCS and thus on maximising economic recovery from these assets. The interviews were used to collect in-depth data on obstacles and opportunities inherent in the UK petroleum taxation system and how this fiscal regime, via decommissioning tax relief and transferability of tax history, may influence ending the lives, or transferring the ownership, of late-life oil and gas assets between operators.

The sample includes all the oil and gas companies that hold exploration and production licences on the UKCS. A list of these companies is available from the NSTA website.[99] The sample also included independent decommissioning consultants, accountants, academics, and professionals from the support and service sectors and the UK Government—all specialists in oil and gas taxation issues. During the summer of 2020, the authors conducted 25 interviews, all of which were audio-recorded, apart from one, during which detailed notes were taken. Interviews were recorded with interviewees' permission, and all the ethical procedures required by the authors' university were followed. Owing to the Covid-19 pandemic and the first UK national lockdown (23 March 2020 to 4 July 2020), interviews were conducted by telephone and online platforms. Table 2 gives information about these interviews.

Table 2

Interview details

Organisation	Code	Job Description	Date of Interview	Years of Experience	Length of Interview	Mode of Interview
Oil and Gas Authority	OGA1	Senior Employee	16.06.2020	26	50 min	Telephone
	OGA2	Decommissioning Manager	01.07.2020	10	67 min	MS Teams
Oil and Gas Companies	OGC1	Tax adviser	11.06.2020	30	27 min	Telephone
	OGC2	International Tax Manager	02.07.2020	12	60 min	MS Teams
	OGC3	Tax Director	03.07.2020	13	60 Min Recording was not permitted	MS Teams
	OGC4	Chief Executive	24.07.2020	10	38 min	MS Teams
	OGC5A	Asset director for North Sea Assets	06.08.2020	21	60 min	MS Teams

[99] These data remain available at NSTA, "Licence data", *https://www.nstauthority.co.uk/data-centre/data-downloads-and-publications/licence-data/* [Accessed 8 September 2022].

	OGC5B	North Sea Operations' Finance Partner		15		
	OGC6	Decommissioning Director	18.08.2020	30	31 Min	MS Teams
	OGC7	Partner & Director	23.08.2020	Not disclosed	33 min	MS Teams
Decom North Sea	DNS1	Interim Managing Director	01.06.2020	11	72 min	MS Teams
	DNS2	Business Development Director	24.06.2020	20	53 min	MS Teams
Oil & Gas Technology Centre (OGTC)	OGTC1	Decommissioning Manager	10.07.2020	26	39 min	MS Teams
Oil & Gas UK	OGUK1	Sustainability Director at Oil and Gas UK, OGUK	22.06.2020	10	50 min	MS Teams
Accounting and Auditing Firms (Big 4)	AAF1	Partner (responsible for oil and gas transactions business)	05.06.2020	23	32 min	MS Teams
	AAF2	Head of Energy	09.06.2020	32	80 min	MS Teams
Academics – Professors	ACA1	Director of a Decommissioning Centre	08.06.2020	15	24 min	MS Teams
	ACA2	Professor of Law at a Scottish University	30.06.2020	10	60 min	MS Teams
UN Extractive Tax Committee	UNETC1	Member of the UN Extractives' Tax Sub-committee	26.06.2020	40	31 min	MS Teams
Decommissioning Operators	DecOp1	Owner of a Decommissioning Company	02.06.2020	37	95 min	Skype
	DecOp2	Chief Commercial Officer	06.07.2020	25	43 min	MS Teams
Independents Decommissioning and Tax Consultants	DecCon1	Director of Decommissioning	03.06.2020	15	37 min	MS Teams
	DecCon2	Director of Own Consultancy Company	03.06.2020	24	64 min	MS Teams
	DecCon3	Freelance Consultant in the Oil Industry	14.06.2020	23	63 min	Telephone
	DecCon4	Associate Director	15.06.2020	17	28 min	MS Teams
	DecCon5	Director of Own Consultancy Company	08.07.2020	15	75 min	MS Teams

(5) Analysis and discussion

The recorded interviews were transcribed verbatim and the transcripts were analysed using NVivo 12 software, commonly used for the analysis of qualitative data, especially interview transcripts.

Interviewees are referred to generally as decommissioning experts, by their role title or by the codes shown in Table 2 to maintain confidentiality and anonymity. An inductive qualitative thematic data analysis was used,[100] with the research questions and sub-questions forming a priori themes and sub-themes for coding purposes. These are used to present the analysis of results, as below.

(a) Research question 1: To what extent does the current UK petroleum fiscal regime affect transfers of ownership of late-life oil and gas assets between operators on the UKCS?

Three decommissioning experts (DecCon5; DNS2; OGC4) believed that the complexity of the UK petroleum taxation system in general was a real obstacle in the way of transfer of asset ownership. In this context, a decommissioning consultant (DecCon5) warned that:

> "This perfect storm of Covid-19, oil price drop, late-life nature of the basin, onerous tax system, onerous regulatory regime, could accelerate the end."

(i) Research question 1(i): What impact do decommissioning tax relief and transferability of tax history have on extending or ending the life of oil and gas fields on the UKCS?

1. Impact of decommissioning tax relief

Decommissioning tax relief was not initially intended to facilitate transfer of late-life assets between operators (AAF1; OGA1). In fact, decommissioning tax relief was seen as an obstacle to new entrants to the UKCS oil business. This is because, if a new company wanted to invest in the UKCS, it would not benefit from a tax relief since it would not have had sufficient tax history by the time of decommissioning a late-life asset and therefore would not be entitled to decommissioning tax relief (DecCon2). Decommissioning relief deeds, by guaranteeing decommissioning tax relief at 50 per cent, allowed companies to save on the costs of guarantees for decommissioning liabilities, with a reduction from 100 per cent to 50 per cent (OGA1). Decommissioning relief deeds and the transferability of tax history made an impact on transferring late-life assets between operators on the UKCS (UNETC1; DecCon2; OGA2). However, two decommissioning experts (DNS1 and OGA2) saw that the valuation gap of the decommissioning tax relief between buyers and sellers was actually a real obstacle to deals. Therefore, the government could provide an assurance to companies that the sum of decommissioning tax relief to which they would be entitled should a transfer take place would enhance the transfer of assets between operators significantly (AAF2).

2. Impact of transferability of tax history

Interviewees appreciated that transferability of tax history was an incentive, and sometimes a "deal breaker", for changing ownership of late-life assets on the UKCS. Without transferability of tax history, decommissioning tax relief blocked the transfer of late-life assets on the UKCS (OGA1): "the lack of it killed a whole load of deals" (AAF2). Transferability of tax history was an enabling mechanism (OGC7; DecCon3), as it allowed more flexibility than previously (ACA1). Two decommissioning experts (DNS1 and DecCon2) saw that the transferability of tax history and decommissioning relief deed had together created a substantial breakthrough as they increased the confidence of new operators so that, in the event of them not having sufficient tax history to claim full decommissioning tax relief, they could still benefit from decommissioning tax relief. An Oil & Gas sustainability director (OGUK1) acknowledged that transferability of tax history was helpful and a driver for a number of deals, but not for every deal. Whilst an oil and gas company executive and Big Four accounting firm partner (OGC5A and AAF1 respectively) both expected that transferability of tax history would enhance transferring assets on the UKCS, other experts (OGC2 and DecCon5) suggested that transferability of tax history could have been better designed with more security for operators. A senior employee with the Oil and Gas Authority (OGA1) suggested that it had had a minimal impact on transferring assets between

[100] Jodi Aronson, "A pragmatic view of thematic analysis" (1995) 2(1) *The Qualitative Report* 1.

operators and was not a necessary change to the tax legislation in the first place. However, contrary to the latter expert's view (i.e. OGA1).

(ii) Research question 1(ii): What barriers may prevent the transfer of late-life oil and gas assets between operators on the UKCS?

The interviewees asserted that transferring ownership of late-life assets faced a number of barriers, some of which were linked to finance, for example, the provision of decommissioning security notes (AAF2; OGA2; DecCon2). Other barriers were linked to the negative view of hydrocarbon production taken by institutional investors who are steering away from oil and gas investments (DecCon2; OGTC1; DNS1; DNS2). Furthermore, additional barriers to transferring ownership of late-life-assets discussed by interviewees were: the increased cost of both production (DecCon1; OGC5A) and maintenance of late-life assets (OGC5B); the sharp decrease in oil price (DecOp2; OGC5B; DecCon2); environmental lobbying against hydrocarbon production (OGC2; UNETC1); societal pressure due to the misunderstanding of the impact of decommissioning tax relief on taxpayers (OGC2)[101]; lack of information and integrity of data related to late-life assets for potential buyers (DecOp2; OGC5A; DNS1; DNS2); decommissioning tax relief and the valuation gap (OGA2; DecCon3; DecCon4); the regulatory regime (OGC7); the "no clean break", and the concept of liability in perpetuity, with regard to sections 29, 31 and 34 of the Petroleum Act 1998 (DecCon3; AAF1; DecCon4; DNS2; OGA1); and, technical failure of an asset (for example, equipment failure which is uneconomic to repair), such as in the case of the Maureen field (DecCon3).

The 2020–21 Covid-19 pandemic has caused international and national economies to slow down and this has, in turn, slowed down technological advancement and investments in late-life oil and gas assets (DecCon1; DecCon2), thus impacting on transfers. Furthermore, opportunities to invest elsewhere and the limited remaining oil and gas reserves on the UKCS are considered to be barriers for enhancing transfer of late-life assets in the UK (ACA2). The transition to "net zero" may also be a significant barrier here, for obvious reasons.

(iii) Research question 1(iii): What risks may the Exchequer incur as a result of an enhanced transfer of late-life assets on the UKCS? If any, how can these risks be dealt with?

In general, transfer of ownership of late-life oil and gas assets occurs between a large operator and a smaller company. Almost all of the interviewees saw a risk in the transfer of ownership of late-life assets because small companies are generally less financially capable and secure, compared with large operators, as far as paying for decommissioning was concerned (AAF1; OGA1; DecCon5).[102] Furthermore, transferring assets was seen as risky owing to a systematic move on the part of large operators out of the UKCS (OGC7; OGC5A; OGC2). However, another decommissioning expert (DNS2) saw that transferring ownership of late-life assets might reduce the risk as the new operators might take different approaches to operating and decommissioning the assets, thus reducing the risk to the Exchequer.

Despite agreeing in the main that there was a level of risk to which transferring late-life assets might expose the Exchequer, interviewees also confirmed that there had not been any case where taxpayers had to pay for decommissioning an oil and/or gas asset on the UKCS (OGC7; OGA2). Interviewees mentioned cases where operating companies/fields had become insolvent, but nonetheless taxpayers had not been exposed to the decommissioning bill, for example, in the cases of the Endeavour Co, Tuscan Energy Co, the Ardmore field, MCX Co in the Dunlin oil field and Fairfield on the

[101] Baxter, "Why is decommissioning not a cost to taxpayer?" *Energy Voice*, 14 November 2019; Williamson, "North Sea oil and gas decommissioning cost estimate cut by billions amid efficiency drive" *The Herald*, 3 July 2019.

[102] See Aldersey-Williams, "Decommissioning security" in Antonas and Hammerson (eds), *Oil and Gas Decommissioning: Law, Policy, and Comparative Practice* (2016).

Murchison platform. Owing to sections 29, 31 and 34 of the Petroleum Act 1998, in none of these cases did liabilities fall back to the taxpayers.

In order to mitigate risks and protect taxpayers from being exposed to decommissioning liabilities, interviewees suggested that the UK Government should establish a decommissioning fund. Companies involved in exploration and production investments on the UKCS would contribute annually to this fund, with the amount of contribution being equal to the provision that companies would accrue to their accounts for decommissioning costs.[103] Such a fund would remove the necessity for "liability in perpetuity" (DecCon1; OGC7). Furthermore, if the liability in perpetuity concept was to be retained, then possibly the "no clean break" should be extended to apply to other corporate entities such as legal and financial organisations that have a stake in oil and gas projects on the UKCS (OGC7). Moreover, to mitigate risks, the state could, possibly, opt to take on the decommissioning liabilities for an agreed payment (ACA2).

(iv) Research question 1(iv): What benefits does transferring the ownership of late-life assets on the UKCS bring to the Exchequer?

Extending the lives of fields via the transfer of ownership offers enhanced petroleum production, security of supply (OGC2; DecOp2; AAF1), job security (DecCon2) and revenues in the form of petroleum-related taxes, national insurance contributions, business rates, value added tax (VAT), income taxes, etc (AAF2; OGC5A; OGC7; DecCon1).

A key benefit for the Exchequer of transferring ownership of late-life assets is the delay in decommissioning (UNETC1; OGC2; OGUK1), as such a delay means delaying the tax rebate (in the form of decommissioning tax relief), which is a considerable sum of money.[104] Delaying decommissioning offers a potential reduction in decommissioning costs via the use of enhanced technologies (OGC1) and the development of expertise and skills (DecCon1): "then the amount of tax reimbursement that comes with decommissioning would be lower as well" (AAF1). An oil company director (OGC2) also argued that transferring ownership of late-life assets, which leads to enhanced production, offered environmental benefits.

An Oil and Gas Authority professional (OGA1), however, took a more conservative approach when judging the benefits that might accrue to the Exchequer from extending late-life assets, as they believed that returns on late-life assets would not be significant, owing to their size and maturity and exposure to fluctuations in oil and gas prices.

From the above analysis, it can be shown that transferability of tax history is an enabling mechanism in the unlocking of decommissioning tax relief in cases of transferring ownership of late-life assets on the UKCS. Despite the risks inherent in transferring assets to smaller operators, the taxpayer seems to be well protected by the "no clean break" concept. Transferring late-life assets between operators offers a number of benefits to different stakeholder groups, and unlocks resources, thus offering tax revenues. However, transferring ownership of late-life assets is subject to a number of difficulties that require addressing. If operators of marginal fields find other investment opportunities elsewhere, they might prefer not to invest more in these fields, hence larger operators, if denied transfer opportunities, would prefer to shut down and decommission the assets and recover tax paid in order to support investment elsewhere.

[103] See Parente et al, "Offshore decommissioning issues: Deductibility and transferability" (2006) 34(15) *Energy Policy* 1992. The UK Government would manage this fund and undertake the decommissioning of the fields. Adjustments could be made where companies pay less/more than the actual cost of decommissioning.

[104] See also Kaiser, "Accounting for offshore structure retirement obligations: Process and factor description" (2005); OGA, *Estimates of the Remaining Exchequer Cost of Decommissioning UK Upstream Oil and Gas Infrastructure (August 2019)* (2019).

(b) Research question 2: What impact would the transfer of late-life assets have on Maximising Economic Recovery?

Interviewees agreed that transferring ownership of late-life oil and gas assets extended the economic lives of these assets and enhanced their net present value (NPV) and production, which in turn enhanced job security, energy security, tax take and thus maximised economic recovery from these fields (AAF1; AAF2; OGC2; OGC7; DecOp2). A number of interviewees (OGC5A; DecCon3; OGC6; OGTC1; ACA1), asserted that transferring ownership of late-life assets to smaller operators, resulting in the "right assets in the right hands", allowed for the meeting of the NSTA objective of Maximising Economic Recovery. This was because those operators, in addition to bringing their competitive advantages (OGUK1) and cost saving skills (DecCon2; UNETC1), had lower operating costs when compared with the major operators such as BP and Shell.[105] Also, transferring assets between operators allows "that innovative thinking of putting different ideas to play" (DecCon5), and thus enhanced production and revenues to stakeholders. However, while an Oil and Gas Authority professional (OGA2) argued that transferring ownership of late-life assets did in principle enhance Maximising Economic Recovery, this did not occur in every case as other factors, such as oil prices and technology, played roles in achieving this objective.

The interviewees offered a number of examples where transferability of ownership had occurred and led to Maximising Economic Recovery. One key example that was mentioned by a number of interviewees was the Forties oil field, which was transferred from BP to the Apache oil company. The Forties field was discovered by BP in 1970 but, owing to a lower estimate of remaining reserves in the field, a lower production of 25,000 barrels a day, and BP having priority investments elsewhere, it was sold to Apache in 2003 (AAF2) after BP had initially lost interest in Forties.

> "Apache actually turned Forties round big time. It went from 25,000 barrels a day to 80,000 barrels a day within two years; the whole way they depleted the reservoir was different" (OGC2).
>
> "They were drilling wells that BP had decided weren't economic and weren't worth drilling" (DecCon2).[106]

Based on the above discussion, the authors argue that it is to the benefit of stakeholders, including the UK Government, to encourage transfer of late-life assets on the UKCS. Such transfer does, however, encounter a number of barriers, as discussed above. Therefore, it would be helpful for policymakers to reduce these barriers in order to stimulate transferability, and extend the lives of these assets, and thus Maximise Economic Recovery.

(c) Research question 3: What impact would Maximising Economic Recovery have on UK petroleum tax revenues?

Given the smaller size of the remaining reserves left in mature fields on the UKCS, the authors were interested in assessing the impact of the Maximising Economic Recovery objective on tax revenues for the nation arising from transferring ownership of these assets. Generally speaking, the interviewees agreed that Maximising Economic Recovery of late-life assets brought petroleum taxes, and other taxes in the form of income taxes and VAT, to the Exchequer (OGC7; DecCon1; AAF1; DecCon4). An oil and gas company tax adviser (OGC1) argued that extending the lives of late-life assets allowed the UK Government to collect, in addition to tax on petroleum production, income tax and taxes from support sectors; also, to defer decommissioning tax relief payments to the industry.

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[105] See Parente et al, "Offshore decommissioning issues: Deductibility and transferability" (2006) 34(15) *Energy Policy* 1992.

[106] Other examples included Chrysaor Ltd buying the Armada gas field from Shell Oil in 2018 (ACA1; OGTC1). The Dunlin oil field was acquired by Fairfield in 2008 from Shell Oil (OGTC1). Also, Wytch Farm, the largest onshore field in Western Europe, was acquired by the Perenco company from BP in 2011 (DecCon5; OGC4).

Although Maximising Economic Recovery results in enhancing tax revenues to the Exchequer, a senior employee of the Oil and Gas Authority (OGA1) argued that the sum of tax revenues accruing to the UK Government from Maximising Economic Recovery from late-life assets was not significant, suggesting that the Maximising Economic Recovery objective is not tax driven.

(d) Research question 4: What other tax reforms could be offered by the UK Government to delay decommissioning late-life oil and gas assets and encourage transfer of these assets between operators?

Given the perceived impact of transferring ownership of late-life assets on Maximising Economic Recovery and on revenues to the UK Government, and based on the view that the UK Government should take a lead on encouraging and supporting such transfers, the interviewees were asked what tax reforms could be offered by the UK Government to delay decommissioning and enhance transfers. The interviewees suggested a number of reforms that could possibly allow enhancement of investments, thus delaying decommissioning. An international tax manager with an oil and gas company (OGC2) suggested that giving security on the transferability at the point of sale would enhance transferring deals between operators. A colleague (OGC7) suggested introducing a tax relief to small companies that buy late-life assets. However, the issue here would be in defining "small". In order to stimulate small and marginal fields, tax incentives are required (OGC5A).

A North Sea operations' finance partner, working for an oil and gas company (OGC5B) suggested expanding the ring-fence concept so that losses from outside the current ring-fenced projects could be included, thus reducing the tax burden on companies. An oil and gas company freelance consultant (DecCon3) argued that, in order to reduce information gaps between buyers and seller, the taxation system and the NSTA needed to offer some mechanisms to enhance transparency regarding decommissioning tax relief. If this were to happen, another decommissioning expert (DNS1) argued that "then [it] will at least narrow down the differences and create a greater possibility of more deals happening". An accounting firm expert in this area (AAF1) contended that:

> "Everything that is done to simplify the tax can help to extend a decision to continue, and things that enable assets to be transferred more tax efficiently might also help to extend the lives of late-life assets in the UKCS."

A number of interviewees thought that the current taxation system is good (for example, AAF2), and that not much could be done by the UK Government to simplify it any further (for example, OGC1). An independent decommissioning expert (DecCon2) agreed with other views expressed (by OGC1) that nothing much can be done, although the latter stated that "there's some minor tweaks but I don't think there's anything major". However, they then suggested that introducing a 100 per cent tax allowance on exploratory wells and reducing the corporation tax rate from 30 per cent to 20 per cent would possibly enhance extending investments on the UKCS in general and in late-life assets in particular, a point that an oil and gas company director also made (OGC7). However, since oil and gas prices have increased significantly following the Covid-19 pandemic, the UK Government introduced EPL at 25 per cent to capture a share of the "super" profit accruing to the industry. The extent to which EPL discourages transferring late-life assets between operators in the UKCS is a practical question for future studies to address.

(e) Research question 5: Is decommissioning tax relief perceived as a government contribution towards decommissioning costs of oil and gas assets or a tax refund for tax overpaid by oil/gas companies?

The interviewees' perceptions were sought on the nature of the decommissioning tax relief and whether they saw it as a government contribution towards decommissioning costs of oil and gas assets on the UKCS or a tax refund of overpayments made by companies during the economic lives of their fields. Every interviewee reiterated that decommissioning tax relief was a refund and a rebate rather than a tax relief/contribution (OGC5A; AAF2). For example, a North Sea assets' director (OGC5A) asked:

> "If the asset has not paid any taxes and we have to decommission it, will Government pay 30 per cent or 50 per cent? No. They are paying only if there is a tax history."[107]

In the same vein of argument, Derek Leith, a senior EY tax partner, concluded that:

> "Decommissioning tax relief is thus a necessary and integral part of the North Sea tax regime, and isn't any kind of 'subsidy' towards the producing companies' decommissioning costs".

Since the UK petroleum fiscal regime does not allow deductions of provisions for decommissioning costs or depreciation of these costs over fields' economic lives (as noted above), it allows the UK Government to over-collect taxes from companies during the lifetime of their reservoirs (OGC2). Administering decommissioning tax relief, and the issue of it being a tax refund, rather than a governmental contribution towards decommissioning costs of oil and gas assets, raises concern about the fairness of the UK petroleum taxation system in relation to decommissioning costs.[108] This emerged overall as a prominent theme concerning the fairness of the UK petroleum fiscal regime and policy. Using the term "tax relief" to describe the repayment of tax was criticised frequently by interviewees, as they considered it to be a tax rebate which therefore should have been termed as such (OGC5B; DecCon2).[109] In their view, using the word "relief" was negative and put the UK oil industry in a difficult position where it sounded as if the UK Government was contributing towards the industry's decommissioning expenses when this was not the case (OGC5A). The theme of fairness was all pervasive. Owing to certain conditions applied when claiming decommissioning tax relief,[110] a decommissioning director with an oil and gas company (OGC6) spoke of a situation where his/her company was concerned about losing a significant sum of tax relief/rebate:

> "We've got about £1.4 billion worth of unclaimed tax relief…I don't know if it's unique, but it's quite a big pot of tax that we'd be looking to relieve on, and we can't do that at the moment, with the production that we have; we'll never get that relief."

One decommissioning expert (DecCon4) criticised the fairness of the decommissioning tax relief from a cash flow perspective. They argued that repaying the tax paid takes more than 24 months after decommissioning costs are paid by an operator, which puts pressure on operators' cash flow, particularly the smaller operators (also noted by DecCon5). Therefore, the repayment should take no more than 12 months. The Head of Energy at a Big Four accountancy (ACA2) claimed that the mechanism of decommissioning tax relief lacked fairness since companies overpay tax during the economic life of their reservoir and are entitled to claim this overpayment back after they decommission a field and encounter loss of operations. A related point made by another decommissioning expert (DecCon2) was that a company can only claim decommissioning tax relief when it makes a loss.[111] Therefore, as argued by the oil and gas company decommissioning director above (OGC6), a company with a profitable portfolio of fields may not be able to claim its overpaid tax. Furthermore, a senior employee with the Oil and Gas Authority (OGA1) clarified that decommissioning tax relief is a company, not field-based allowance, and is capped by the tax history that a company has. Whilst companies are entitled to claim decommissioning tax relief against any PRT payments, their claims against RFCT and the SC are capped up to March 2002. This means any overpayment of RFCT made by a company before that date is not refundable, which casts doubts on the fairness of the UK petroleum tax regime.

[107] See HM Treasury, *Tax Issues for Late-Life Oil and Gas Assets: Discussion Paper* (2017).
[108] See Parente et al, "Offshore decommissioning issues: Deductibility and transferability" (2006) 34(15) *Energy Policy* 1992.
[109] See also Leith, "North Sea decomm tax relief broken down" (2017).
[110] See HMRC, *Oil and Gas Taxation: Transferable Tax History and Retention of Decommissioning Expenditure* (2020), paras 2.9 and 2.10.
[111] See Parente et al, "Offshore decommissioning issues: Deductibility and transferability" (2006) 34(15) *Energy Policy* 1992.

(6) Conclusion

The analysis reveals that transferability of tax history legislation is expected to make a difference in enhancing transfer of late-life oil and gas assets between operators on the UKCS and therefore allows the Maximising Economic Recovery objective of the NSTA to be achieved. Whilst such transfers offer a number of benefits, such as enhancing energy security, securing jobs and tax take for the UK Government, several barriers may hold back such transfers. Lack of finance, the fiscal regime and regulations and public perceptions/opinions are some of these barriers. In order to enhance transfers, the UK Government could offer some measures to enhance transparency and trust that would facilitate smoother transfers. Despite these benefits and barriers, the authors conclude that, owing to the "no clean break" concept, transferring ownership to smaller operators, does not expose taxpayers to significant risk of being liable for decommissioning costs of oil and gas assets.

The analysis reveals also that transferring ownership of late-life assets delays decommissioning, delays the payment of decommissioning tax relief by the UK Government and offers an opportunity for innovative technology and models to reduce decommissioning costs. It is clear that decommissioning tax relief is never a tax relief/contribution by the UK Government towards decommissioning costs of oil and gas assets on the UKCS, but a tax rebate of tax previously overpaid. The mechanism and administration of the decommissioning tax relief raise concerns about the fairness of this element of the UK petroleum taxation system. The authors conclude that the way in which decommissioning tax relief is managed does not offer fairness to the operators and stress in this regard the cash flow issue for operators, particularly smaller operators. However, it is understandable that in order to offer the taxpayer a higher level of protection from being exposed to decommissioning liabilities of oil and gas assets, the current taxation system is appropriate. Nevertheless, of key concern are the several issues that militate against the concept of the inherent fairness of the system. Such issues include the fact that provisions for decommissioning costs cannot be deducted for tax and the fact that a company needs to be experiencing financial loss arising from the decommissioning before it can be eligible to claim decommissioning tax relief, hence the time lag in obtaining a refund of tax that has, effectively, been overpaid.

The UK Government has set a target where greenhouse gas emissions are to be brought to "net zero" by 2050. Furthermore, in response to increased oil prices following the Covid-19 pandemic, the UK Government introduced EPL at 25 per cent. The Maximising Economic Recovery objective in relation to the UKCS oil and gas resources involves enhancing production from these resources. Such production is associated with emissions arising during, exploring for, extracting, transporting, refining and consuming these resources. The EPL reduces the profits of oil and gas companies and may disincentivise investments in oil and gas projects. Therefore, it is important to consider the sustainable policy options and fiscal measures that allow for such a transition whilst maintaining the Maximising Economic Recovery objective and the UK's energy security. The UK petroleum fiscal regime has been subject to many changes since its first establishment in 1964, giving rise to an instability that seems to mirror the changeability of the British weather. Incentivising investments in the UKCS requires simplifying and stabilising the UK petroleum fiscal regime.