

Summary: Intervention & Options

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| Department /Agency: HM Treasury and HM Revenue and Customs | Title: Impact Assessment of change to Petroleum Revenue Tax obligations. | |
| Stage: Implementation | Version: 1 | Date: Budget 2008 |
| Related Publications: : Securing a Sustainable Future: A Consultation on the North Sea Fiscal Regime | | |

Available to view or download at:

http://www.hm-treasury.gov.uk/consultations_and_legislation/consult_liveindex.cfm

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What is the problem under consideration? Why is government intervention necessary?

Under the Petroleum Revenue Taxation (PRT) regime all fields liable to PRT are required to make a PRT return. However many fields, although liable to PRT, neither pay, nor are ever likely to pay PRT. The completion of PRT returns therefore represents an unnecessary administrative burden. There is also a question as to whether the existence of PRT on these fields has a negative impact on investment decisions, even though PRT is not actually paid. Following the legislative changes made in 2006 concerning the valuation of North Sea oil sold other than at 'arms length' it has also become apparent that elements of certain of the PRT returns (PRT 1A in particular) are no longer necessary, and again continuing to require such information represents an unnecessary administrative burden.

What are the policy objectives and the intended effects?

Reduction in unnecessary information and administrative obligations placed on companies operating fields subject to PRT and in the burden of form filling. Facilitation of asset trade and investment through removing from the PRT regime those fields never likely to pay PRT.

What policy options have been considered? Please justify any preferred option.

- 1) Do nothing and persist with collecting information that is no longer required, and imposing an obligation that is never likely to result in the payment of tax.
- 2) Act now to remove redundant information obligations, and to lift an administrative burden in respect of fields that may never pay PRT.

When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects?

The impact of the proposed policy measures is likely to be included in any review of the measures implemented following the HM Treasury December 2007 Consultation on North Sea Taxation.

Ministerial Sign-off For final proposal/implementation stage Impact Assessments:

I have read the Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) the benefits justify the costs.

Signed by the responsible Minister:

Angela EagleDate: 24 February 2008

Summary: Analysis & Evidence

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|-----------------------|---------------------|
| Policy Option: | Description: |
|-----------------------|---------------------|

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|---|---|---|
| COSTS | ANNUAL COSTS | Description and scale of key monetised costs by 'main affected groups' |
| | One-off (Transition) Yrs | |
| | £ - | |
| | Average Annual Cost (excluding one-off) | |
| £ - | Total Cost (PV) | £ |
| <p>Other key non-monetised costs by 'main affected groups' Some costs may be incurred by companies in dismantling their existing PRT obligation systems, and by others in amending their systems to exclude information previously required for the PRT1A returns.</p> | | |

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| BENEFITS | ANNUAL BENEFITS | Description and scale of key monetised benefits by 'main affected groups' |
| | One-off Yrs | |
| | £ 0 | |
| | Average Annual Benefit (excluding one-off) | |
| £ 50K - 100K | Total Benefit (PV) | £ 75k |
| <p>Other key non-monetised benefits by 'main affected groups' Savings arising from the removal of fields from the scope of PRT (the timing and extent of which will depend on whether and when agreements can be reached with the various participating companies).</p> | | |

Key Assumptions/Sensitivities/Risks Estimate of the saving from PRT1A made with reference to the PRT administrative costs contained in the Standard Cost Model. Some 60 of the 100 or so pre March 1993 PRT liable fields are currently not paying tax because their gross profits are covered by expenditure, allowable losses, or oil allowance.

| | | | |
|-------------------------|----------------------|--|---|
| Price Base Year 2005 | Time Period Years | Net Benefit Range (NPV) £ 50k - 100k | NET BENEFIT (NPV Best estimate) £ 75k |
|-------------------------|----------------------|--|---|

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|---|----------------------|-------|--------|-------|
| What is the geographic coverage of the policy/option? | UK Continental Shelf | | | |
| On what date will the policy be implemented? | Royal Assent 2008 | | | |
| Which organisation(s) will enforce the policy? | HMRC | | | |
| What is the total annual cost of enforcement for these organisations? | £ | | | |
| Does enforcement comply with Hampton principles? | Yes | | | |
| Will implementation go beyond minimum EU requirements? | N/A | | | |
| What is the value of the proposed offsetting measure per year? | £ 0 | | | |
| What is the value of changes in greenhouse gas emissions? | £ 0 | | | |
| Will the proposal have a significant impact on competition? | No | | | |
| Annual cost (£-£) per organisation (excluding one-off) | Micro | Small | Medium | Large |
| Are any of these organisations exempt? | No | No | N/A | N/A |

| | | | |
|---|----------------------|-----------------------|---------|
| Impact on Admin Burdens Baseline (2005 Prices) | | (Increase - Decrease) | |
| Increase of £ 0 | Decrease of £ 75k | Net Impact | £ - 75k |

Key: Annual costs and benefits: Constant Prices (Net) Present Value

Evidence Base (for summary sheets)

Rationale for intervention

The UK Government remains committed to promoting a healthy and prosperous UK oil and gas industry and has a stated objective to maximise the economic recovery of the UK's oil and gas reserves. Whilst the underlying geology and future oil and gas prices are the dominant drivers of investment, and hence ultimate recovery, Government has a crucial role to play in ensuring that the fiscal regime helps deliver the best possible future for oil and gas production from the UK Continental Shelf (UKCS). A careful balance must be struck between promoting investment and production, whilst ensuring a fair return for the UK taxpayer from our national resources.

Following the 2005 Pre-Budget report the Government has engaged with the oil and gas industry and other interested stakeholders to discuss wider structural concerns over areas of the North Sea fiscal regime which were viewed as running counter to the above policy objectives. Following those discussions Government is undertaking a package of reforms to the North Sea fiscal regime to help encourage investment, reduce the impact of the fiscal regime on investment decisions, help facilitate asset trade, increase certainty and stability, remove anomalies and simplify the fiscal regime and reduce the administrative burden it imposes. This measure forms part of that package.

Policy Objective

Conversations on the wider future of the Petroleum Revenue Tax (PRT) regime are still ongoing between Government and industry as part of the wider discussions on the North Sea fiscal regime. However despite this Government believes that where appropriate changes should be made to the existing regime to ensure that it is effective and efficient and continues to meet the Government's objectives for the North Sea fiscal regime. For the changes outlined here the objective is to simplify the PRT regime by reducing companies' administrative obligations and decreasing the compliance burden. As part of the ongoing conversations with industry over the future of PRT it has also become clear that for those fields that are liable to PRT, but do not, nor are expected ever to, pay due to the system of reliefs and allowances, there are still perceived barriers to asset trading and investment. Government has therefore sought to create a mechanism whereby such fields can be removed from PRT altogether.

Policy proposals

Petroleum Revenue Tax was abolished for fields given development consent on or after 16 March 1993. A number of fields that were given development consent before that date, whilst falling within the PRT regime, will never actually pay any PRT during their productive life. This is because of the interaction of the various reliefs and allowances within the regime.

HMRC has recognised the compliance burden this imposes on companies that have interests in such fields (the legislation refers to them as 'participators'), in so far as they are required to comply with the mechanics of the PRT regime, via the various returns, whilst not actually being PRT-payers. In recent years HMRC has reduced the regulatory requirements on such companies by allowing companies to defer submitting returns where, because of the lack of practical tax impacts, neither HMRC nor the companies would obtain any benefit from the submission of the returns.

However companies have made the point that despite the relaxed regulatory regime, the potential liability for PRT remained as long as the company was a taxable field for PRT purposes and that this had some impact on asset transfers.

The proposal therefore is, that where the participators can satisfy HMRC that they will be 'never payers' in the future in respect of particular fields (usually because of the amount of oil allowance available to them), that HMRC will make such fields non-taxable fields for PRT purposes. There will, of course, be circumstances where participators wish to stay within the scope of PRT even if they are not going to pay tax on a particular field, for example in order that they can utilise any unrelievable field losses generated. In such situations, the fields will remain within PRT.

The other changes relate to the amount of information that is required on PRT returns submitted to HMRC. Form PRT1A is one of a number of returns that participators in a field are required to complete and submit to HMRC (the information required on the return is listed in section 62 Finance Act 1987). As a result of legislation enacted in Finance Act 2006, oil produced in the North Sea was split into two categories – Category 1 and Category 2. The change in the law means that HMRC only now requires information on Category 2 oils from companies when they complete form PRT1A. We therefore wish to amend section 62 FA 1987 to reflect this. This will result in compliance savings for the companies, inasmuch as they have to submit less information to HMRC and also provide for processing savings for HMRC.

Benefits

The Government expects there to be an on-going annual total North Sea industry compliance saving in respect of the removal of 'Category 1' oils from the PRT 1A return (available at www.hmrc.gov.uk/forms/prt1a_booklet.pdf) until such time as the relevant fields cease production.

The compliance savings is estimated to be between £50k - £100k, giving rise to a central figure of £75k. The basis for estimating the cost saving is a 2006 study, based on the Standard Cost Model methodology, into the administrative burdens on businesses. The relevant report on PRT can be found at <http://www.hmrc.gov.uk/better-regulation/part20.pdf>. These reports itemise the administrative burdens in various ways, including by form type, and it has been possible from an analysis of the underlying granular data to derive an estimate for the cost to companies of completing the PRT 1A, and hence make an estimate of the saving to companies in respect of no longer having to report 'Category 1' oils. These oils are known to account for the bulk of transactions reported on the PRT1A.

There are also likely to be savings arising from the removal of fields from the scope of PRT. But the timing and extent will depend on whether and when agreements can be reached with the various participating companies and it is therefore not possible to put a precise figure on what the savings might be across the industry as a whole on an annual basis.

Costs

Some small one-off costs may be incurred by companies in dismantling their existing PRT obligation systems, and by others in amending their systems to exclude 'Category 1' oils as previously required on PRT1A returns. However the Standard Cost Model does not provide a means for estimating what such one-off costs might be, albeit that they are likely to be modest in relation to the accumulating annual savings.

Consultation

In the 2005 Pre-Budget report the then Chancellor announced that the Government would open discussions with the oil and gas industry to examine wider structural concerns over areas of the North Sea fiscal regime. These discussions would cover any areas of the fiscal regime which either Government or industry felt could potentially undermine ongoing stability, and impact on the Government's objective to maximise the economic recovery of the UK's oil and gas reserves.

The initial round of discussions lasted from January 2006 though to September 2006 and provided a forum within which UKCS stakeholders could discuss any aspect of the fiscal regime with officials from HM Treasury, HM Revenue and Customs and BERR. A large number of stakeholders took advantage of this opportunity and meetings were held with a wide range of delegates from oil and gas companies, representative bodies, academics, the supply chain and other stakeholders.

At Budget 2007 Government published "The North Sea Fiscal Regime: a discussion paper". This discussion paper summarised the discussions that had occurred up to September 2006, and set out the conclusions that had been drawn from those. It also announced that discussions would continue, with the paper forming the basis for further, more focussed discussions through to the end of September 2007.

The issues outlined above were raised during the two rounds of discussions. The Government's proposals to remedy those were then set out in "Securing a sustainable future: a consultation on the North Sea Fiscal Regime" that was released in December 2007. Where possible draft legislation was

published alongside the consultation document to allow interested parties to comment on the exact detail of the proposed measures. The consultation period lasted through to the end of January 2008.

Competition Assessment

These proposed changes will reduce the compliance cost disparity between North Sea oil and gas fields subject to PRT and those fields outside its scope. The removal of potentially PRT paying fields from PRT will also facilitate the sale of North Sea assets by removing uncertainty over future liability to PRT.

Small Firms' Impact Test

There are no small businesses involved in North Sea oil and gas extraction that are affected by Petroleum Revenue Tax.

Specific Impact Tests: Checklist

Use the table below to demonstrate how broadly you have considered the potential impacts of your policy options.

Ensure that the results of any tests that impact on the cost-benefit analysis are contained within the main evidence base; other results may be annexed.

| Type of testing undertaken | <i>Results in Evidence Base?</i> | <i>Results annexed?</i> |
|----------------------------|----------------------------------|-------------------------|
| Competition Assessment | Yes | No |
| Small Firms Impact Test | Yes | No |
| Legal Aid | No | No |
| Sustainable Development | No | No |
| Carbon Assessment | No | No |
| Other Environment | No | No |
| Health Impact Assessment | No | No |
| Race Equality | No | No |
| Disability Equality | No | No |
| Gender Equality | No | No |
| Human Rights | No | No |
| Rural Proofing | No | No |