



**HM Revenue
& Customs**

Capital Allowances for Oil Decommissioning Expenditure

Draft legislation and Explanatory Note
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Contents**Page**

	Introduction	3
Chapter 1	Draft legislation	4
Chapter 2	Explanatory Note	9

Introduction

In today's Budget, the Government announced that it was amending, with immediate effect, the rules providing tax relief for the decommissioning costs of North Sea installations and infrastructure. The changes ensure that companies can claim tax relief for decommissioning costs only for the accounting period in which the work is actually carried out.

This document provides the draft legislation and Explanatory Notes in relation to the changes that have been made.

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Chapter 1

This section contains the current draft of the legislation.

Capital allowances for oil decommissioning expenditure

Schedule 1 contains provision about capital allowances for oil decommissioning expenditure.

SCHEDULE 1

CAPITAL ALLOWANCES FOR OIL DECOMMISSIONING EXPENDITURE

- 1 CAA 2001 is amended as follows.
- 2 (1) Section 163 (meaning of “general decommissioning expenditure”) is amended as follows.
 - (2) In subsection (1), for “(3) and (4)” substitute “(3) to (4)”.
 - (3) After subsection (3) insert—
 - “(3A) The expenditure must have been incurred wholly or substantially in complying with—
 - (a) an approved abandonment programme,
 - (b) a condition to which the approval of an abandonment programme is subject, or
 - (c) a condition imposed by the Secretary of State, or an agreement made with the Secretary of State—
 - (i) before the approval of an abandonment programme, and
 - (ii) in relation to the decommissioning of the plant or machinery.”
 - (4) In subsection (5)(b), at the beginning insert ““abandonment programme”, “approval” and “approved” (in relation to an abandonment programme)”.
- 3 (1) Section 164 (general decommissioning expenditure incurred before cessation of ring fence trade) is amended as follows.
 - (2) For subsection (1) substitute—
 - “(1) A person (“R”) carrying on a ring fence trade may elect to have a special allowance made to R for a chargeable period (the “relevant chargeable period”) if conditions A and B are met.
 - (1A) Condition A is that one or more of these paragraphs applies—
 - (a) R incurs general decommissioning expenditure in the relevant chargeable period in respect of decommissioning carried out in that period;
 - (b) R incurs general decommissioning expenditure in the relevant chargeable period in respect of decommissioning carried out in a previous chargeable period;
 - (c) R incurred general decommissioning expenditure in a previous chargeable period in respect of decommissioning that has not been carried out until the relevant chargeable period.
 - (1B) Condition B is that the plant or machinery concerned has been brought into use for the purposes of the ring fence trade.”

- (3) In subsection (2)(a), for the words from “the chargeable period” to the end substitute “the relevant chargeable period, and”.
- (4) In subsection (3) –
- (a) in paragraph (a), omit “and”,
 - (b) after paragraph (a) insert –
 - “(aa) the chargeable period in which the expenditure was incurred,
 - (ab) the decommissioning to which the expenditure relates,
 - (ac) the chargeable period in which the decommissioning was carried out, and”.
- (5) In subsection (4)(a), for the words from “the chargeable period” to the end substitute “the relevant chargeable period, and”.
- (6) In subsection (5), for the words from “a chargeable period” to the end, substitute “the relevant chargeable period is equal to the amount of the general decommissioning expenditure to which the election relates.”
- (7) After subsection (5) insert –
- “(5A) But subsection (5) is subject to subsections (5B) and (6).
 - (5B) If an amount of general decommissioning expenditure to which the election relates is disproportionate to the relevant decommissioning carried out in the specified decommissioning period then, for the purposes of this section, the election is to be taken to specify only the allowable expenditure.
 - (5C) The application of subsection (5B) to an amount of general decommissioning expenditure does not prevent a person from making an election under this section for a subsequent chargeable period specifying the non-allowable expenditure.
- (5D) In subsections (5B) and (5C) –
- “allowable expenditure”, in relation to general decommissioning expenditure, means the amount of the expenditure that is proportionate to the relevant decommissioning carried out in the specified decommissioning period;
 - “non-allowable expenditure”, in relation to general decommissioning expenditure, means so much of that expenditure as is not allowable expenditure;
 - “relevant decommissioning”, in relation to general decommissioning expenditure, means the decommissioning to which the expenditure relates;
 - “specified decommissioning period”, in relation to relevant decommissioning, means the chargeable period specified in the election as the period in which the decommissioning was carried out;
 - “specified expenditure period”, in relation to general decommissioning expenditure, means the chargeable period specified in the election as the period in which the expenditure was incurred.”

- 4 (1) Section 165 (general decommissioning expenditure after ceasing ring fence trade) is amended as follows.
- (2) In subsection (1), for paragraph (b) substitute –
“(b) the decommissioning condition is met in relation to a notional accounting period, and”.
- (3) After subsection (1) insert –
“(1A) The decommissioning condition is met in relation to a notional accounting period (the “relevant period”) if one or more of these paragraphs applies –
- (a) the former trader incurs general decommissioning expenditure in the relevant period in respect of decommissioning carried out in that period;
 - (b) the former trader incurs general decommissioning expenditure in the relevant period in respect of decommissioning carried out in –
 - (i) a previous notional accounting period, or
 - (ii) a chargeable period falling before the first notional accounting period;
 - (c) the former trader incurred general decommissioning expenditure in –
 - (i) a previous notional accounting period, or
 - (ii) a chargeable period falling before the first notional accounting period,in respect of decommissioning that has not been carried out until the relevant period.

- (1B) “Notional accounting period” means each of the following periods –
- (a) the period that –
 - (i) begins with the day following the last day on which the former trader carried on the ring fence trade, and
 - (ii) ends with the day on which the first termination event subsequently occurs;
 - (b) each period that –
 - (i) begins with the day following the last day of a period determined under paragraph (a) or this paragraph, and
 - (ii) ends with the day on which the first termination event subsequently occurs;

but there are to be no notional accounting periods after the end of the post-cessation period.

- (1C) “Termination event”, in relation to a notional accounting period, means each of the following –
- (a) the end of the period of 12 months beginning with the first day of the notional accounting period;
 - (b) the occurrence of an accounting date of the former trader or, if there is a period for which the former trader does not make up accounts, the end of that period (but see subsections (6A) and (6B));
 - (c) the end of the post-cessation period.”

- (4) In subsection (3) –

- (a) after “applies” insert “in relation to a notional accounting period”, and
- (b) in paragraph (a), after “relevant decommissioning cost” insert “for that period, or the aggregate of all the relevant decommissioning costs for that period,”.

- (5) In subsection (4), for the definition of “the relevant decommissioning cost” substitute –

““relevant decommissioning cost”, for a notional accounting period, means the amount by which general decommissioning expenditure falling within paragraph (a), (b) or (c) of subsection (1A) in relation to that period exceeds any amounts received before or during that period for the remains of any plant or machinery on whose demolition any of the general decommissioning expenditure was incurred.”

- (6) After subsection (4A) insert –

- “(4B) If an amount of general decommissioning expenditure is disproportionate to the relevant decommissioning carried out in the decommissioning period then, for the purposes of this section, only the allowable expenditure is to be taken to have been incurred in the expenditure period.
- (4C) The application of subsection (4B) to an amount of general decommissioning expenditure does not prevent the non-allowable expenditure from being taken into account under this section in relation to a subsequent notional accounting period.

(4D) In subsections (4B) and (4C) –

“allowable expenditure”, in relation to general decommissioning expenditure, means the amount of the expenditure that is proportionate to the relevant decommissioning carried out in the decommissioning period;

“decommissioning period”, in relation to relevant decommissioning, means the notional accounting period or chargeable period in which the decommissioning was carried out;

“expenditure period”, in relation to general decommissioning expenditure, means the notional accounting period or chargeable period in which the expenditure was incurred;

“non-allowable expenditure”, in relation to general decommissioning expenditure, means so much of that expenditure as is not allowable expenditure;

“relevant decommissioning”, in relation to general decommissioning expenditure, means the decommissioning to which the expenditure relates.”

(7) After subsection (6) insert –

“(6A) If the former trader –

(a) carries on more than one trade,

(b) makes up accounts of any of them to different dates, and

(c) does not make up general accounts for the whole of the company’s activities,

subsection (1C)(b) applies with reference to the accounting date of such one of the trades as the former trader may determine.

(6B) If the Commissioners for Her Majesty’s Revenue and Customs are of the opinion, on reasonable grounds, that a date determined by the former trader for the purposes of subsection (6A) is inappropriate, the Commissioners may by notice direct that the accounting date of such other of the trades referred to in that subsection as appears to the Commissioners to be appropriate is to be used instead.”

5 This Schedule has effect in relation to expenditure incurred on or after 22 April 2009.

Chapter 2

This section contains the Explanatory Note based on the draft legislation.

SUMMARY

1. The Clause and Schedule amend the rules providing for tax relief for decommissioning costs to ensure that companies can claim relief for decommissioning costs only for the accounting period in which the work is actually carried out. The Government has become aware of arrangements that have been entered into which seek to establish a claim for tax relief for decommissioning costs several years in advance of any decommissioning work being carried out. These arrangements are an attempt to undermine the integrity of the North Sea ring fence. The change will have effect in relation to decommissioning costs incurred on or after 22 April 2009.

DETAILS OF SCHEDULE

2. Paragraph 2 amends section 163 of the Capital Allowances Act 2001 (CAA) to provide that general decommissioning expenditure must be incurred wholly or substantially to comply with an approved abandonment programme, or conditions associated with the approval of an abandonment programme. Sub-paragraph (3) inserts new subsection (3A) to this effect.
3. Paragraph 3 extends and amends section 164 of CAA to provide that the costs allowable for relief will be those costs of the accounting period that relate to the decommissioning work that is actually carried out in the accounting period.
4. New subsection 164 (1A) provides that Condition A applies in one or more of the situations where R incurs general decommissioning expenditure in the relevant chargeable period in respect of decommissioning –
 - (a) carried out in that period;
 - (b) carried out in a previous chargeable period; or
 - (c) that has not been carried out until the relevant chargeable period.
5. Sub-paragraph (4) inserts new subsections (3)(aa), (ab) and (ac) into section 164 of CAA which provide what an election to have a special allowance must also specify.
6. Sub-paragraph (7) inserts new subsections (5A), (5B), (5C) and (5D) into section 164 of CAA.
7. New subsection (5B) provides that if the general decommissioning expenditure is not proportionate to the decommissioning work carried out in the chargeable period, then only the expenditure that is proportionate will be allowable.
8. New subsection (5D) provides, for subsections (5B) and (5C), definitions of “allowable expenditure”, “non-allowable expenditure”, “relevant

decommissioning”, “specified decommissioning period” and “specified expenditure period”.

9. Paragraph 4 amends section 165 of CAA to provide for notional accounting periods within the post-cessation period.
10. Sub-paragraph (3) inserts new subsections (1A), (1B) and (1C) into section 165 of CAA.
11. New subsection (1A) provides that the decommissioning provision is met in relation to a notional accounting period if the former trader incurs general decommissioning expenditure in the relevant period in respect of decommissioning carried out in certain periods.
12. New subsection (1B) provides the meaning of “notional accounting period” for periods within the post-cessation period.
13. New subsection (1C) provides the meaning of “termination event” in relation to a notional accounting period.
14. Sub-paragraph (5) substitutes in section 165(4) of CAA a revised definition of “relevant decommissioning cost”
15. Sub-paragraph (6) inserts new subsections (4B), (4C), and (4D) into section 165 of CAA.
16. New subsection (4B) provides that if the general decommissioning expenditure is not proportionate to the decommissioning work carried out in the decommissioning period, then only the expenditure that is proportionate will be allowable.
17. New subsection (4D) provides, for subsections (4B) and (4C), definitions of “allowable expenditure”, “decommissioning period”, “expenditure period”, “non-allowable expenditure” and “relevant decommissioning”.
18. Sub-paragraph (7) inserts new subsections (6A) and (6B) into section 165 of CAA.

BACKGROUND NOTE

19. Companies that are party to North Sea licences for the production of oil and gas have a legal obligation to decommission installations and structures within those licensed areas at the end of the field’s productive life.
20. Companies have to fully meet the costs of decommissioning but do obtain tax relief for all of those costs, which they can set against their ring fence corporation tax and supplementary charge profits.
21. Relief for decommissioning costs is given through the capital allowances legislation which provides that where a person is carrying on a ring fence trade and incurs general decommissioning expenditure, a special capital allowance is available, equal to the whole amount of decommissioning expenditure that is incurred in the period in question.

22. The Government has become aware of arrangements that have been entered into which seek to establish a claim for tax relief for decommissioning costs several years in advance of any decommissioning work actually being carried out. This undermines a fundamental general principle that relief is given in the accounting period, for costs incurred in respect of the work actually carried out in that accounting period.
23. The proposed change addresses this situation by ensuring that tax relief for decommissioning costs will only be given in respect of those costs that relate to the work actually carried out in the accounting period.