Policy paper

Energy Taxes Factsheet

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Autumn Statement 2022: summary of changes to oil and gas profits taxation

- From 1 January 2023, the rate of the Energy Profits Levy will be increased to 35% to ensure oil and gas companies benefitting from extraordinary prices pay their fair share.
- To continue encouraging companies to reinvest their profits in the UK, we will maintain the existing cash value of the levy's investment allowance, ensuring there is still a significant increase in relief compared to the permanent system. To achieve this, the rate of the allowance will be reduced from 80% to 29% for all investment expenditure besides decarbonisation expenditure. The allowance will remain at 80% for decarbonisation expenditure (defined as investment in carbon emissions reducing technology) such as installing bespoke wind turbines to power the production installation.
- In addition to this, a new and temporary tax of 45% will be introduced on the extraordinary profits of electricity generators who, like the oil and gas sector, have seen profits increase well above their company predictions

What is the Energy Profits Levy?

- The Energy Profits Levy was introduced on 26 May 2022 to help fund more cost-of-living support for UK families.
- Demand for energy post COVID-19 and the invasion of Ukraine by Russia have meant oil and gas prices have risen substantially since last year with gas prices in 2022 reaching unprecedented levels.
- Prices, and in turn profits, are expected to remain high among oil and gas producers for the foreseeable future.
- The Energy Profits Levy, which currently places a 25% charge on these profits, ensures oil and gas producers pay their fair share. This is in addition to the permanent 40% tax rate paid by oil and gas producers, taking the combined headline tax rate for the sector to 65%.

What part of the Energy Profits Levy is changing?

- Today [17th November] we are announcing that from the start of 2023 the Energy Profits Levy will increase by 10% points to 35%.
- We have also confirmed that the levy will remain in place until the end of March 2028 providing companies with the certainty they need to plan and take investment decisions.
- This will bring the headline tax rate for the sector to 75% which is comparable to other North Sea tax regimes, including Norway.
- This ensures oil and gas companies benefitting from the prolonged period of increased prices continue to pay their fair share of tax towards restoring public finances and helping to contribute to cost-of-living support.
- Before these changes, the levy was expected to raise around £20 billion through to 2025-26. Taken together, both of these changes are expected to raise just under £20 billion more over the next six years raising just over £40 billion in total.
- The government will also no longer consider phasing out the levy ahead of its end date of March 2028, giving companies greater certainty to plan their investments.
- In total we expect the oil and gas sector to pay around £80 billion in tax over the next six years.

How will the Energy Profit Levy's investment allowance change?

- The government has always been clear that it wants to see the oil and gas sector reinvest its profits to support the economy, jobs, and the UK's energy security.
- The energy profits levy included a 'super-deduction' style relief which aimed to encourage companies to invest in UK oil and gas extraction, putting more UK gas on the grid for longer, supporting jobs and the economy and bolstering the future energy security of the UK.
- This 80% Investment Allowance meant businesses would get a £91.25 tax saving for every £100 they invest – providing them with an additional incentive to invest. This nearly doubled the tax relief available and means the more investment a firm makes, the less tax they will pay.
- Under the 35% levy rate, the government is reducing the rate of the allowance to 29% which, due to the higher rate, will broadly maintain the existing cash value of the allowance.
- This means business will be able to claim £91.40 in tax relief for every £100 invested rather than the previous £91.25
- We also recognise the crucial role oil and gas firms in helping us to achieve our ambitious net zero targets by investing in world leading renewable infrastructure and green energy products.
- The government has always been clear that it wants to see the sector reinvest its profits to further support Net Zero, domestic jobs and the UK's energy security. The Net Zero Strategy also recognised that remaining oil and gas installations will use low carbon power, with the sector currently working towards reducing emissions by 25% in 2027 and by 50% in 2030.
- To encourage this, decarbonisation expenditure such as modifying existing installations to use power from offshore windfarms, installing bespoke wind turbines to power the installation or running electricity cables to the installation from shore will continue to qualify for the current investment allowance rate of 80%.
- This means from the 1st of January 2023, a company spending £100 on upstream decarbonisation will now be able to deduct £109.25p when calculating its levy profits. The example below shows how this works:

Tax	Tax rate	Relief	Relief rate	Amount of relief (for £100 investment in expenditure)	Amount of (for £100 decarbonis investment
Ring Fence Corporation Tax	30%	First year capital allowance	100%	30	30
Supplementary Charge	10%	First year capital allowance	100%	10	10
Supplementary Charge	10%	Investment allowance	62.5%	6.25	6.25
Total tax relief under the permanent regime				46.25	46.25
EPL	35%	First year capital allowance	100%	35	35
EPL	35%	Investment allowance	29% (for expenditure)/80% (for decarbonisation expenditure)	10.15	28
Additional tax relief under EPL				45.15	63.00
Total tax relief				91.40	109.25

What about the Electricity Generator Levy?

- The structure of the electricity market means the price of electricity is tied to the wholesale gas price and, as a result, many electricity generators are also seeing extraordinary returns by the unprecedented increase in gas prices.
- To ensure that electricity generators also pay their fair share towards strengthening public finances and supporting households and businesses get through the current cost of living challenges, we are introducing a new, temporary 45% levy on these extraordinary profits, defined as electricity sold above £75MWh.
- This is approximately 1.5 times the average price of electricity over the last decade.
- Combined with corporation tax, this brings the cumulative rate on earnings over £75Mwh to 70%.
- This levy will also replace the Cost Plus Revenue Limit announced in October. The new levy is a more proportionate measure that is not only administrable through the corporate tax system which generators are familiar with but will leave generators with a greater proportion of their returns to invest in growing the UK's renewable energy capacity.
- Many countries have taken, or are in the process of taking, steps to reduce or claw-back extraordinary returns being realised by low-carbon generators. That includes France, Italy and Spain that have all introduced some form of ex-post price cap on low carbon generation or introduced a tax on their excess returns.
- Unlike the Energy Profits Levy which applies to all profits, only returns above the set benchmark of £75MWh are within scope. Due to this, the rate for the levy is being set higher than the levy on oil and gas producers.
- By applying to only the extraordinary and unforeseen profits the Electricity Generator Levy will minimise any increase to underlying business costs.
- This is expected to raise over £14 billion between 2023 and 2028 and will help pay for the more than £55 billion of support being provided for household and business energy bills.
- The levy will apply from 1 January 2023 and will be legislated for in in the next Finance Bill.
- The temporary and proportionate levy is not expected to harm long term investment due to it applying to only a portion of excess profits and electricity generators still being able to write off their investments against corporation tax by deducting their investment spending from their profit.
- The tax will not apply to electricity that is generated under a Contract for Difference entered into with the Low Carbon Contracts Company Ltd (LCCC).

Further facts and background

- There is precedent for taxes on exceptional profits. For example, in 1981, a one-off tax on certain bank deposits was introduced via a 2.5% levy on deposits of banking businesses, who were benefiting from high interest rates.
- The oil and gas sector pay a 40% headline rate of tax on profits, this breaks down to a 30% Ring Fence Corporation Tax and a 10% Supplementary Charge.
- The permanent 40% headline tax rate for oil and gas producers is competitive globally against similar operating environments, and is lower than Norway, the Netherlands and Denmark. The Energy Profits Levy is an additional tax which reflects the extraordinary global context of high oil and gas prices.
- The rate increase and changes to the investment allowance will take effect from the beginning of 2023.
- The government will legislate for the Autumn Statement measures in Autumn Finance Bill 2022, except the changes related to decarbonisation expenditure which will be legislated for in Spring Finance Bill 2023.
- Companies will still be unable to offset previous/historic losses or decommissioning expenditure against profits subject to the Energy Profits Levy.
- The North Sea will continue to remain the foundation of the UK's energy security during the transition to net zero and maintaining investment is key.
- This is why we will be consulting stakeholders over the coming months as part of a review of the UK's long-term tax treatment of the North Sea after the Energy Profits Levy ceases to ensure the regime delivers predictability and certainty, supporting investment, jobs and country's energy security. The review will report by the end of 2023.