The Energy Profits Levy (EPL)

Summary

- The EPL is a temporary 25% (35% from 1 January 2023) tax on the profits of oil and gas companies operating in the UK and the UK Continental Shelf. From 26 May 2022 until 31 March 2028, it increases the headline rate of tax on those profits from 40% to 65% (75% from 1 January 2023). The new levy has built in a new investment allowance which will reward those companies who invest in oil and gas production. The rate of the allowance is 80% (falling to 29% from 1 January 2023 consistent with the higher rate of EPL). See also here.

How does the Energy Profits Levy work?

- The EPL is an additional tax on UK oil and gas profits on top of the previous 40% headline rate of tax (comprising Ring fence Corporation Tax [RFCT] at 30% and Supplementary Charge [SC] at 10%), taking the combined rate of tax on profits to 65% (75% from 1 January 2023).

- To tax the extraordinary profits appropriately, companies are not able to offset previous losses or decommissioning expenditure against profits subject to the levy.

How does the new Investment Allowance work?

- In contrast to the SC investment allowance, that can be claimed only once income is received from the field subject to the investment (which can take several years), the new Investment Allowance for the EPL is available to companies at the point of investment, making it both more immediate and more generous for companies with current taxable profits.

- 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 EPL is an additional tax which reflects the extraordinary global context.

- 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 original 80% EPL Investment Allowance.

How the tax operates

The EPL is charged at 25% (35% from 1 January 2023). The tax base is computed in a similar manner to RFCT and SC.

The levy applies to a company’s ‘ring fence profits’, computed with a number of adjustments, and is charged as if it were an amount of corporation tax.

The adjustments are:

- finance costs are left out of account. This mirrors the provision that exists for the calculation of adjusted ring fence profits for SC.

- decommissioning costs are left out of account. This ensures that extraordinary profits are not reduced by decommissioning expenditure.

- an investment incentive. An ‘allowance’ will be generated on investment expenditure (capital expenditure and some operating and leasing expenditure) at 80% (29% from 1 January 2023) which can be used immediately to reduce profits subject to the levy. This allowance operates similarly to the SC investment allowance, but a key difference is that the allowance generated is not required to be activated by relevant income and can be used to create or augment a levy loss. As with the SC investment allowance, there are restrictions on the generation of allowance on the acquisition of an asset which has already been in receipt of allowances in the ring fence.
- loss relief is available within the EPL, but there is no cross over to any other ring fence taxes. Levy losses are capable of being relieved through i) carry back of 12 months against previous levy profits (3 years for terminal losses), ii) carried forward to set against future levy profits, and iii) group relief in-year to another company in the group with levy profits.
- RFCT losses cannot be used to reduce profits subject to the EPL. No historic losses are allowed to be carried forward into the levy regime. This ensures that levy profits are not reduced by historic losses. Loss relief for RFCT and SC remains unchanged.

Additional boxes will be added onto the CT600 to report levy profits and how much levy is payable, and companies will be required to submit information on the amount of levy payable.

Annex: The remaining UK oil and gas tax regime

The UK oil and gas fiscal regime taxes profits earned by companies from the production of oil and gas on the UK Continental Shelf. The regime is kept separate to other taxes on commercial profit by the operation of a “ring fence” which prevents losses from other activities being imported into the regime. The pre-EPL headline rate of tax was 40%, made up of the following taxes:

- 30% Ring Fence Corporation Tax – this is a tax on profits from exploration and production in the UK, largely on the same basis as normal corporation tax rules. This rate has not changed since the Supplementary Charge was introduced in 2002.
- 10% Supplementary Charge – this is an additional charge of 10% on adjusted ring-fence profits, excluding finance costs. It has remained unchanged since 2016 (when it was reduced from 20% to 10%). The rate peaked at 32% between 2011 and 2014.
- 0% Petroleum Revenue Tax – a field-based tax charged on profits arising from fields given development consent before 16 March 1993. It has been zero-rated from 2016 but not abolished to allow companies to carry back trading and decommissioning losses.