HM Treasury

ENERGY PROFITS LEVY FACTSHEET: 26 May 2022

- Following record high oil and gas prices over the past year due to global circumstances, and to help fund more cost-of-living support for UK families, the government is introducing the Energy Profits Levy, a new 25% surcharge on the extraordinary profits the oil and gas sector is making.
- Oil and gas prices have risen substantially, with oil prices nearly doubling since early last year, and gas prices more than doubling, resulting in significant increases in profits earned from UK oil and gas extraction.
- The new Energy Profits Levy will raise around £5 billion over the next year which will go towards supporting people with the new cost of living measures announced by the Chancellor.
- The government has also 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.
- That's why, within the levy, a new 'super-deduction' style relief is being introduced to encourage firms to invest in oil and gas extraction in the UK.
- The new 80% Investment Allowance will mean businesses will overall get a 91p tax saving for every £1 they invest – providing them with an additional, immediate incentive to invest. This nearly doubles the tax relief available and means the more investment a firm makes, the less tax they will pay.
- The levy does not apply to the electricity generation sector. However, certain parts of it have also seen extraordinary profits partly due to record gas prices. As set out in the Energy Security Strategy, the government is consulting with the power generation sector and investors to drive forward energy market reforms and ensure that the price paid for electricity is more reflective of the costs of production. Those reforms will take time to implement. In the meantime, the government will urgently evaluate the scale of these extraordinary profits and the appropriate steps to take.

How will the Energy Profits Levy work?

- Currently, the oil and gas sector pay a 40% headline rate tax on profits consisting of 30% Ring Fence Corporation Tax and 10% Supplementary Charge.
- In recent years, under the existing regime, fewer than 35 groups have made tax payments each year. In 2021, the top 7 groups accounted for around 95% of payments.
- The Energy Profits Levy is an additional 25% tax on UK oil and gas profits on top of the existing 40% headline rate of tax, taking the combined rate of tax on profits to 65%.
- To appropriately tax the extraordinary profits, companies will not be able to offset previous losses or decommissioning expenditure against profits subject to the levy.
- It is expected to raise around £5 billion in its first 12 months.
- The tax will take effect from today, 26 May 2022, and will be legislated for via a standalone Bill to be introduced shortly.
- In future years, if oil and gas prices return to historically more normal levels, the Government will phase out the Energy Profits Levy, and also the legislation will include a sunset clause, effective at the end of December 2025.

How the new Investment Allowance will work?

- The government has also been clear that it wants to see the oil and gas sector reinvest their profits to support the economy, jobs and the UK's energy security.
- To encourage this, a 'super-deduction' style investment allowance will be introduced within the levy to provide an immediate incentive for the oil and gas sector to invest in UK extraction.
- The new investment allowance rate is 80% and means the total tax relief on investment nearly doubles - for every £1 businesses invest they will overall get a 91p tax saving.
- The current 10% Supplementary Charge provides companies with an investment allowance that can only be claimed once income is received from the field subject to the investment (which can take several years).
- In contrast, the new 80% Investment Allowance for the Energy Profits Levy will be available to companies at the point of investment, making it both more immediate and more generous.
- The government expects the combination of the levy and this investment allowance to lead to an overall increase in investment, and the OBR will take account of this policy in their next forecast.

Overall, the tax relief companies receive from qualifying expenditure will nearly double, from 46p for every £1 of extra investment to 91p

The example below shows how this works for an assumed £100 of capital expenditure.

	Tax rate	Relief	Relief rate	Amount of relief (assuming £100 investment)
Ring Fence Corporation Tax	30%	First year capital allowance	100%	30
Supplementary Charge	10%	First year capital allowance	100%	10
		Investment allowance[1]	62.5%	6.25
Total tax relief under current scheme				46.25
Energy Profits Levy	25%	First year capital allowance	100%	25
		Investment allowance[2]	80%	20
Additional tax relief under new scheme				45
Total tax relief under new scheme				91.25

[1] This can be claimed when the investment starts generating income.

[2] Unlike the Supplementary Charge investment allowance, this can always be claimed in the first year (i.e. in the year of investment expenditure).

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 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.

Existing 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 current headline rate of tax is 40%, made up of the following taxes:

- 30% Ring Fence Corporation Tax (RFCT) – this is a tax on profits from exploration and production in the UK, largely on the same basis as normal corporation tax rules. This has not changed since the Supplementary Charge was introduced in 2002.
- 10% Supplementary Charge (SC) – 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 losses arising from trading and decommissioning.