International Tax

Norway Tax Alert

9 May 2013

Tax increase announced for petroleum companies

Contacts

Petter Gruner
pgruner@deloitte.no

Rolf Saastad
rsaastad@deloitte.no

On 5 May 2013, the Norwegian government announced proposed changes to the petroleum tax system that include reducing the "uplift" from 7.5% to 5.5%, which would result in a reduction in the overall uplift (i.e. for four years) from 30% to 22%. Also announced was a reduction in the general corporate income tax rate from 28% to 27%, but for petroleum companies, this rate reduction would be offset by an increase in the rate of the special petroleum tax from 50% to 51%. If approved, the changes to the tax rates would apply as from 2014 and the changes to the uplift would apply as from 5 May 2013.

Companies that have been granted a license to explore and produce petroleum on the Norwegian continental shelf (and in some cases carry on activities relating to pipeline transportation) are subject to a special petroleum tax regime. The regime has two components: the taxation of profits from petroleum exploitation (and pipeline transportation) at a rate of 28% and a special petroleum tax of 50%. The tax base for calculation of the two taxes generally is the same, except that in calculating the special petroleum tax, an additional deduction (the "uplift) is available. The special tax may not be deducted from the base of the ordinary petroleum tax and vice versa.

The uplift is calculated on costs incurred in connection with the development carried out under a license. Currently, the uplift is calculated as 7.5% of the annual development costs for four years as from the year of the investment, resulting in a total uplift of 30%. If the uplift cannot be utilized in a particular year, it may be carried forward (along with other losses) indefinitely. The uplift has the effect that development costs are ultimately depreciated at the rate of 130% when calculating the base for (future) special petroleum tax liability.

The government has now proposed to reduce the annual uplift to 5.5% (for the four-year period) on costs incurred after 4 May 2013, making the total uplift 22%, i.e. a reduction of eight percentage points. Depending on the discount rates used, the change is likely to cause the after-tax cash investment for the development of a field to increase by at least 10%-15% (assuming 100% equity finance).

Transition rules would apply as follows:

1) Where a plan for development and operations (PDO) is submitted to the Ministry of Oil and Energy (MOE) before 5 May 2013, the reduced uplift

would apply only to development costs incurred during the year following the year production commences;

2) For development costs incurred where an application not to prepare a PDO is made to the MOE before 5 May 2013, the reduced uplift rate would apply only to costs incurred during the year following the year production commences;
3) Where a notification is submitted to the MOE before 5 May 2013 to the effect that there will be substantial deviations from a previously filed PDO and development costs are incurred after the notification is submitted, the reduced uplift rate would apply only to costs incurred during the year following the year in which production commences; and
4) Where the PDO or application/notification mentioned above relates to an additional investment under a production license, the current 7.5% annual uplift would apply to costs incurred up to and including the year in which the additional investment starts producing.

The transition rules in 1) and 2) also would apply to applications submitted to the MOE regarding certain facilities not used in production but still covered by the petroleum tax regime (e.g. pipelines, certain cooling systems, etc.). The current 7.5% uplift would apply to development costs incurred up to and including the year in which the facility becomes operative.

In addition to the direct economic effect the proposals would have on exploration and production companies, they are likely to impact suppliers to such companies since it seems likely that an indirect effect of the proposals could be that investments in some fields that have been considered for development will be postponed or scrapped entirely.