

(Provisional version)

Ministry of Finance

Prop. 113 L

(2019 - 2020)

Proposition to the Storting (bill)

Temporary amendments to the Petroleum Taxation Act

*Recommendation from the Ministry of Finance of 12 May 2020,
approved in the Council of State on the same date.*

(Solberg Government)

Provisional version

1 Introduction and summary

The Government has been requested to «*consider various policy initiatives and submit proposals that may stimulate investment in the oil and gas industry and in the Norwegian supply industry*» no later than in connection with the Revised National Budget for 2020, cf. the Storting's petition resolution no. 474 of 31 March 2020. In the Revised National Budget for 2020, the Government is proposing a NOK 70 million appropriation for seabed mineral surveying under the auspices of the Norwegian Petroleum Directorate. Such surveying will provide this part of the industry with contract opportunities in 2020. In addition, the Government will revert to the Storting with a green restructuring package proposal in late May. The present proposition sets out a proposal for temporary changes to petroleum taxation.

Oil demand has declined sharply in the wake of the coronavirus disease outbreak. This has severely impacted the oil price. The gas price is also low. Operational challenges resulting from infection control measures are causing petroleum companies to defer investment and maintenance. Infection risk is addressed by scaling back offshore crews. The coronavirus disease outbreak and the oil price slump give rise to temporary liquidity and financial challenges, as well as increased uncertainty about future developments. In the absence of temporary tax initiatives, investment activity on the Norwegian continental shelf may undershoot current projections over the next few years due to deferral of planned profitable investment projects. The supply industry has faced a challenging profitability situation for some time and has, like most other industries, incurred additional costs as the result of infection control measures. Businesses will find themselves in an even more precarious situation if the very low oil price causes petroleum companies to significantly scale back anticipated activity.

The Government is of the view that the prevailing situation in the petroleum industry and the supply industry now calls for temporary measures to improve the liquidity of petroleum companies. The measure offers companies improved prospects for going ahead with planned investments. This may serve to keep the supply industry going by expected contracts in relation to new projects being put out for tender. One may thereby counter a negative trend of layoffs, redundancies and, potentially, bankruptcies.

In view of the current situation, the Government is proposing temporary changes to petroleum taxation that will accelerate deductions, thereby deferring tax payments and improving company liquidity. Specifically, the Government proposes immediate deduction of investments in the special tax base, with the addition of 10 percent uplift. The proposal applies to certain specified investments incurred from the income years 2020 up to and including 2024; see Chapter 3.2. It is proposed, furthermore, that payment may be claimed of the tax value of any loss and unused uplift for the income years 2020 and 2021; see Chapter 3.3. Payment of the tax value of loss also provides liquidity for companies that are operating at a loss or recording a loss as the result of early deductions. The Ministry proposes that granting of security interests in the claim for payment of the tax value be permitted. A clarification is also proposed in Section 3 d of the Petroleum Taxation Act on limitation of net financial costs.

The changes will serve to accelerate investment cost deduction and the tax value of negative tax bases will be paid out. Liquidity improvements resulting from the proposal will serve to enable companies to go ahead with investments. The estimated profitability of investments after tax may also increase, depending on what required rate of return is applied by petroleum companies, cf. Box 3.2.

It is estimated that the proposals as a whole will provide petroleum companies with considerable liquidity, in the region of NOK 100 billion for the years 2020 and 2021, cf. Chapter 4. It is estimated that the proposal will increase tax revenues by about NOK 14 billion over time, measured as net present value at a risk-free discount rate. It is emphasised that the estimates are uncertain and will depend on, inter alia, how companies' investments develop.

For petroleum companies that apply a risk-adjusted required rate of return in their valuation of the tax deductions, the Government's proposal will entail a tax reduction over time. The reduction will for example be about NOK 15 billion, measured at net present value if applying a risk-adjusted required real rate of return of 8 percent.

The overall proposal increases administrative burdens for companies and tax authorities, especially inasmuch as there will for several years be two parallel sets of rules for the tax treatment of expenses incurred in acquiring production facilities and pipelines.

The Ministry proposes that the proposal on immediate deduction of costs, with the addition of 10 percent uplift, in the special tax base shall enter into force immediately with effect for the income years 2020 up to and including 2024, cf. Chapter 5. It is proposed that payment of the tax value of loss and unused uplift shall enter into force immediately with effect for the income years 2020 and 2021. The ordinary rules will apply to any costs incurred and any loss and unused uplift arisen subsequent to the said income years. It is proposed that the clarification in Section 3 d of the Petroleum Taxation Act shall enter into force immediately with effect as from the income year 2020.

The proposals on immediate deduction and payment of loss and unused uplift shall apply for a limited period of time, cf. above. The Ministry proposes that the amendments be set out in a temporary provision in the Petroleum Taxation Act. Reference is made to the proposed new Section 11 of the Petroleum Taxation Act. Reference is made, furthermore, to the proposed amendment to Section 3 d, Sub-section 2, of the Petroleum Taxation Act.

2 The current provisions

Companies involved in the extraction and pipeline transport of petroleum on the Norwegian continental shelf are taxed under the special rules in Act of 13 June 1975 No. 35 relating to the Taxation of Subsea Petroleum Deposits, etc. (the Petroleum Taxation Act).

Costs incurred in acquiring pipeline and production facilities, including the installations which form part of, or are related to, such facilities, may be depreciated on a straight-line basis at a maximum rate of 16 2/3 percent per annum, i.e. over six years, cf. Section 3 b,

second sentence, of the Petroleum Taxation Act. The first year of the depreciation period may be the year in which the costs were incurred. The deduction is granted in both ordinary income and the special tax base.

A special deduction; uplift, is granted in determining the special tax base, cf. Section 5 of the Petroleum Taxation Act. The purpose of the uplift is to compensate for investments being depreciated over several years. The uplift is 5.2 percent of the cost price of operating assets that are depreciated pursuant to Section 3 b of the Petroleum Taxation Act (production facilities and pipelines), and is deductible upon the assessment of special tax for four years from the first year of the cost price depreciation period, inclusive. The uplift comes to a total of 20.8 percent of the cost price of the operating asset, on a nominal basis over the uplift period.

Section 3 f and Section 5, Sub-section 5, of the Petroleum Taxation Act set out special rules on realisation or withdrawal of operating assets as referred to in Section 3 b of the Petroleum Taxation Act. The rules are intended to ensure symmetric treatment of depreciation and uplift on the part of the purchaser and divestment taxation on the part of the seller.

If a company does not in any given income year have sufficient income from which to deduct costs (losses) and uplift, any uncovered loss and unused uplift may be carried forward for deduction in subsequent years. Interest is added to the amount carried forward, cf. Section 3 c, Sub-section 2, and Section 5, Sub-section 6, of the Petroleum Taxation Act. Interest is added in order not to reduce the deductible value of the loss when the loss is carried forward to subsequent income years, thereby furthering equal tax treatment of companies that are in a tax paying position (i.e. companies that in any income year have income from which costs can effectively be deducted) and companies that are not in a tax paying position (i.e. companies that will only obtain effective deduction of costs in any future income).

If the company's loss is caused by exploration expenses, the company may alternatively claim annual payment from the State of the tax value of the exploration expenses (exploration reimbursement). The tax value is determined by multiplying the deductible exploration expenses in ordinary income and in the special tax base by the applicable tax rates for the year in which the exploration expenses are incurred. The amount is determined by the tax authorities for the relevant income year, cf. Section 3 c, Sub-section 5, of the Petroleum Taxation Act.

A company that upon the discontinuation of its petroleum activities on the Norwegian continental shelf still has any uncovered loss or unused uplift to carry forward, may claim payment of the tax value of such uncovered loss and unused uplift from the State, cf. Section 3 c, Sub-section 4, and Section 5, Sub-section 7, of the Petroleum Taxation Act. The tax value is determined by multiplying uncovered loss in ordinary income in the shelf district and in the special tax base by the applicable tax rates at the time of discontinuation, and correspondingly for unused uplift in the special tax base. The amount is determined by the tax authorities for the year in which the taxable activities are discontinued. Alternatively, the company may assign uncovered loss and unused uplift to