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Chief Executive

28 June 2022

The Rt Hon Rishi Sunak MP
Chancellor of the Exchequer
HM Treasury
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Dear Chancellor of the Exchequer

Thank you for visiting Aberdeen last week and meeting members of the UK's oil and gas and energy industry. It was important that we discussed the negative impact of the Energy Profits Levy (EPL) on investor confidence and its likely undermining of our activities here in the UK, both in relation to oil and gas security of supply and underpinning the energy transition. We are keen to continue the dialogue relating to the issues we discussed, and I offer some further reflections as follows:

1. **Restoring Investor Confidence** - There is a critical role for you and HMT to work with industry to help restore long-term investor confidence that has been impacted by the EPL, undermining current and future investment plans and negatively impacting companies borrowing capacity. This is a risk the sector consistently warned about throughout all our engagement with BEIS, HMT and No10. Several companies in the meeting outlined the damage to the UK's competitiveness, particularly in comparison to other jurisdictions which have maintained fiscal stability and are therefore less risky in terms of investment choices. An additional concern relates to uncertainty around whether the levy will indeed be removed at the end of 2025.

As you know, the sector is made up of a diverse range of companies who are all at a different point in their investment cycle, and therefore the introduction of the energy profits levy will have different implications depending on their respective positions. We are aware of instances where borrowing capacity has been reduced by around 15-20%, acutely impacting companies that rely on debt capacity to fund and grow their business. This is exacerbated by the need to provide additional security for decommissioning which could increase by around 15% over the next year, further restricting companies' available capital.

- a. **Time limiting the EPL:** Industry needs certainty that the EPL will be terminated by the end of 2025 at the latest and we would hope that ministerial statements will continue to reinforce the timebound nature of the EPL. Without strong signals to the contrary, industry, investors and their banks will continue to factor the EPL into their long-term economic assessments, constraining access to finance and handicapping UK investment.
- b. **Maintaining the diversity of companies on the UKCS is pivotal to UK energy security:** OEUK is proposing the **introduction of a small profit allowance**, up to a certain threshold, allowing companies' small profit to be exempt from the EPL. This will be particularly important for companies, who have been investing for many years and accumulated significant losses and are now only making marginal profits to help minimise their going concern risk.

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- c. **Recognition for companies who have invested through the “Covid-downturn”:** Separately, recent **capital expenditure arising from 1 Jan 2020, should be deductible** against the energy profits levy. These companies made significant investments despite historically low oil and gas prices (2020 Average - \$42 Oil Price and 25p/therm Gas Price) and are now being adversely and disproportionately affected by the introduction of the EPL.
 - d. **Recognise the need for flexibility** in using the EPL losses and the impact on investment cycles, particularly relating to decisions made in 2024/2025. There is concern that without the ability to carry back losses to the commencement of the EPL, there is a risk that losses will become stranded, and be a disincentive to invest in the latter half of the EPL period.
2. **Supporting decarbonisation of supply** - The oil and gas energy companies are committed to supporting the UK achieve net-zero by 2050. This is central to the North Sea Transition Deal that the sector signed with the UK government in March 2021. Several projects that will be key to the delivery of the emissions commitments within the Deal, such as the electrification of assets, are significantly net-present-value negative. The introduction of the EPL makes these projects even less economic and reduces available capital to be invested in them.

To this end, we propose that decarbonisation projects, such as the electrification of production facilities sanctioned during the EPL window, should benefit from the EPL capital allowance even on expenditure which extends beyond that date. This measure would only be applied to capital expended inside the ring fence. To make this expenditure allowable, it is noted that there must be an extension of the EPL carry back which OEUK proposes is extended to 26th May 2022.

3. **Avoiding double taxation of decommissioning activity** – Decommissioning has a pivotal role in the UKCS asset lifecycle, and the subsequent re-use of assets will help support the energy transition. The current draft legislation has an adverse impact through the inclusion of PRT refunds within the energy profits levy which creates an asymmetry in the regime. We request that the EPL is not applied to PRT refunds relating to decommissioning and have written to your officials with detailed proposals on the changes to the draft legislation and hope you will give this significant consideration recognising to do otherwise will distort the market and could lead to decommissioning being postponed outside the EPL period. The cost of such an approach would be around £150 million over the life of the EPL and would send a powerful reinforcement of commitment by the UK government to helping deliver the energy transition at pace.

We have written separately to your officials and HMRC providing technical commentary on the EPL draft legislation and hope to see these technical points addressed before the bill is published in the House of Commons.

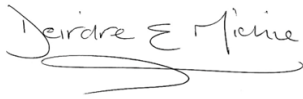
While we remain disappointed at the decision to create the EPL, OEUK and our members want to work constructively with you to help rebuild investor confidence and ensure that the EPL is designed and implemented thoughtfully and is fit for purpose.

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We trust you find the above useful and look forward to regular engagement as agreed at the roundtable on Thursday. Moving forward, ensuring ongoing and regular dialogue at a ministerial level as well as at an official level in HMT, will be critical to helping to rebuild industry and investor confidence in the UK as a place that is open for business so that the sector can continue to play its part in supporting the UK's energy security and support net-zero.

Yours sincerely

A handwritten signature in black ink, reading 'Deirdre E Michie'.

Deirdre Michie OBE
Chief Executive