

Massive public subsidy, minimal public gain.

At the end of May, the Chancellor Rishi Sunak bowed to pressure and introduced a windfall tax on the huge profits being made by North Sea oil and gas companies. At the same time, however, he introduced a generous new tax relief that enables companies to avoid most of the levy if they invest in oil and gas.

Here is what this means for UK energy security, household energy bills and the climate.

Ramping up oil and gas subsidies

The Chancellor's Energy Profits Levy, or windfall tax, imposed an additional 25% tax on oil and gas profits. The new levy will partially fund a £15 billion support package to help UK households struggling with soaring energy bills. From October, nearly every domestic electricity customer in the country will receive a £400 discount off their energy bill under the new measures.

Tied to this levy, however, is a generous tax relief for oil and gas companies. The new Investment Allowance provides a loophole in the windfall tax and means that whatever a company invests in North Sea oil and gas, almost as much (80%) will be discounted from their windfall tax bill. The new allowance is designed to incentivise the industry to invest in new UK oil and gas production. "Our Energy Profits Levy will encourage investment, not deter it," Sunak told Parliament. "The more a company invests, the less tax it will pay."

The new allowance will see oil and gas companies receive overall a 91% tax relief on investments, nearly double the relief previously available, with the majority of it available to companies immediately at the point of investment (as opposed to once the field starts generating income). As the Institute for Fiscal Studies puts it, investing £100 in the North Sea now will cost companies only £8.75. The public will pick up the remaining investment costs (in the form of forgone windfall tax).

The new levy raises the UK's headline tax rate for oil and gas companies from 40% to 65%, still lower than the global average of 70% and for only a short period. The levy's sunset clause of December 2025 (or before if oil and gas prices return to 'historically more normal levels'), means that the UK tax rate will revert back to being one of the lowest in the world. The UK has given North Sea oil and gas companies almost £14 billion in subsidies since signing the Paris Agreement in 2015. This new tax relief will potentially hand an additional £6 billion in public subsidies to oil and gas companies.

The subsidy could also extend to fracking companies, which may be able to claim *even more* tax relief than offshore oil and gas firms under Rishi Sunak's plan. The government is coming under sustained pressure to lift the moratorium on fracking. If it does, the new subsidy could mean that an investment of £100 in fracking will cost companies just £7.50, with the remaining cost paid for by the UK government. While the tax regime is the same for both onshore and offshore oil and gas production, slight differences mean that fracking companies could receive overall a 93% tax relief on investments, slightly more even than the subsidies going to North Sea oil and gas firms.

No benefit to UK households from massive, new oil and gas subsidy

The new subsidy for fossil fuel investment is thought to be worth at least £1.9 billion a year to the oil and gas industry – against the estimated £5 billion the Chancellor hopes to raise from his windfall tax. Yet the public gain from this generous tax giveaway will be minimal. New UK oil and gas production, whether offshore or onshore fracking, will not lead to lower bills, a fact conceded by Ministers.

Jackdaw: paying for North Sea gas twice

Investment by Shell in the newly approved Jackdaw gas field means the oil giant – which recorded record quarterly profits of over £7 billion earlier this year – will pay £210 million less in windfall tax, according to analysis of Rystad Energy data by Uplift.

As a result of this shortfall, the public purse is going to have to cover the recently announced £400 energy bill discount for half a million UK households. Jackdaw's gas reserves, however, will have next to no impact on UK energy bills (the price we pay for gas being set by supply and demand changes globally). The UK public, therefore, will effectively be paying for Jackdaw's gas twice: once in this £210 million subsidy to Shell to develop Jackdaw and again when it's drilled and sold back to us.

Jackdaw's gas reserves will only meet around 1- 2% of UK gas demand on average over its lifetime. It would start producing gas in 2025 and production would drop by almost 60% within four years of its peak in 2026. Jackdaw will not prevent the UK from needing to import gas.

This subsidy could, instead, have been spent on measures to help UK households lower energy costs. For example, the same amount of money over the same period, could have insulated two million homes, which – unlike the oil and gas subsidy – would have reduced the average household bill by £342 a year, and saved 1.8 million tonnes of CO₂ emissions annually.

Minimal benefit to UK energy security from massive, new subsidy

The new Investment Allowance is unlikely to lead to an increase in UK energy security.

First, the geology of the North Sea means that the majority of fossil fuel projects in the pipeline are to extract oil, not gas: analysis by Uplift of Rystad data shows that oil makes up approximately 72% of the resources in planned North Sea investments between now and 2026. But, it's mostly not the type of oil that we use in UK refineries, which means that we export 80% of it.

Pilot oil field: £600 million of public money well spent?

North Sea operator, Orcadian Energy, has plans to develop an oil field, Pilot, 90 miles east of Aberdeen. Orcadian expects the cost of developing Pilot to be “roughly \$1 billion” (£818m).

The firm suggests, however, that its after tax costs to develop Pilot could be reduced by “up to 75%” thanks to the UK’s investment incentives, including the new Investment Allowance. In other words, by investing in Pilot, Orcadian Energy could save itself approximately £614 million on its tax bill. In effect, UK tax payers would subsidising this one oil field to the tune of over £600 million.

Pilot is a crude oil field containing just 79 million barrels of oil, which like 80% of all North Sea oil, would likely be exported overseas. There is almost no public benefit in terms of cheaper fuel bills or energy security from this massive public subsidy.

Second, developing a new field in the North Sea is a complex and lengthy process, conditions that are unaffected by this financial incentive. As a result, the new Investment Allowance will not have a “dramatic effect on investment” over the period of the levy, according to industry analysts. In other words, the new subsidy is unlikely to lead to an increase in UK oil and gas production.

There is a chance, however, that this new subsidy could lead to otherwise economically unviable projects being developed and these becoming stranded assets, with little or no economic value. As the Institute for Fiscal Studies notes: “A massively loss making investment could still be profitable

after tax,” and it is “hard to see why the government should provide such huge tax subsidies and thereby incentivise even economically unviable projects”.

The Investment Allowance should be understood, though, as a loophole to ensure that *existing* investment plans by oil and gas companies are not impacted by the windfall tax. Some of these planned projects may be accelerated to best make use of the Investment Allowance, but it is unlikely to “encourage investment”, the Chancellor’s stated aim.

The subsidy should be seen, therefore, as the Chancellor’s response to threats by oil and gas companies to review planned investments should he seek to claw back too much of their record profits.

Massive climate impact from new oil and gas subsidies

The climate crisis demands urgent action to phase out oil and gas. Multiple warnings have been issued – by the climate scientists, the UN and other international bodies – that there can be no new investment in oil and gas if we are to maintain a liveable climate. Reflecting this, the UK and other countries made a commitment at COP26 to phase out fossil fuel subsidies, a commitment highlighted again in the recent [communique](#) of the G7.

In the region of 33-39 planned North Sea oil and gas projects are likely to be developed in the next three years, the period during which UK taxpayers will effectively be footing 91% of the bill for investment. Approving these projects would create almost 900 million tonnes of greenhouse gases. That’s more than double the net amount of greenhouse gases the UK is estimated to have emitted in 2020, at a time when emissions need to fall dramatically to stay within safe climate limits. Burning Jackdaw’s gas reserves alone would create the equivalent of more than half of Scotland’s annual emissions or Ghana’s entire annual emissions.