1 Introduction and summary

The petroleum deposits on the Norwegian continental shelf are a limited natural resource which belongs to the Norwegian State. These petroleum resources are valuable and provide a foundation for very substantial returns through production, often referred to as resource rent. Together with the State's direct financial interest (SDFI), a special tax helps ensure that a large proportion of this resource rent flows into the public purse.

Norway's petroleum policies are based on the principle that companies make decisions on exploration, development and operations. It is important that the applicable framework conditions are designed to ensure the greatest possible alignment between the assessments of companies and society. Accordingly, the special tax should have a neutral design such that profitability assessments before and after introduction of the special tax are identical. Additionally, the corporation tax payable by petroleum companies should be as similar as possible to the corporation tax paid by companies in other industries. This will facilitate optimal exploitation of available petroleum resources and generate large revenues for the public purse. Investment levels will remain high for many years to come, and the design of the special tax will thus continue to play a very significant role.

A neutral special tax will incentivise companies to refrain from investment in unprofitable projects. In Official Norwegian Report (NOU) 2018:17, the Climate Risk Commission recommended adopting a neutral design for the petroleum taxation system based on a climate risk perspective.

The Government considers 2022 to be a good start date for improving the petroleum taxation system. The temporary tax rules introduced in the spring of 2020 are due to be phased out from 2022 onwards, and companies will again have to apply the ordinary tax rules.

The Ministry is proposing to restructure the special tax as a cash-flow tax with immediate expensing of new investments. The proposal only applies to investments made in the 2022 tax year or later which are taxed under the ordinary rules. The temporary rules will be phased out gradually in line with the relevant resolution of the Storting (the Norwegian parliament).

This change will render the special tax neutral and thus ensure alignment of corporate and societal assessments, provide predictability about future tax rules and give companies a considerable liquidity injection, thereby reducing their capital needs. The longstanding discussion about how future investment deductions should be valued for special tax purposes will be ended. The new system will be similar to the regime already introduced for hydropower with effect from 2021.

The Ministry is proposing that immediate expensing in the special tax system should also apply to costs incurred when acquiring production installations and pipelines, which are currently depreciated pursuant to section 3b of the Petroleum Taxation Act. Immediate expensing is a unique feature of the special tax regime. No changes are proposed to the corporation tax depreciation rules.

Once investment costs can be deducted immediately, there will no longer be any need for the current uplift, which is intended to compensate the taxpayer for the fact that investment deductions are spread out over time. The uplift will therefore be eliminated. Equally, the deduction of financial costs linked to investments which are expensed in full will no longer be needed. In technical terms, most of the deduction will lapse when the residual tax value of the operating assets falls to zero.

The Ministry is proposing that companies should benefit from settlement of the special tax value of losses as of the 2022 tax year. This will strengthen the liquidity of companies without taxable income, which would otherwise have to carry losses forward with an interest supplement. The proposal envisages that settlement will occur at the time of tax assessment, as under the current exploration cost tax refund scheme. Appropriate settlement checks are important. The Ministry therefore considers that the system of negative advance tax instalments, which is included among the temporary rules adopted by the Storting in the spring of 2020, is not suitable for inclusion in a system designed to apply for the longer term. Based on consultation feedback, the Ministry will consider proposing a system for pledging loss settlements, as currently found in the exploration tax cost refund scheme. Two current special tax arrangements – the exploration cost tax refund and the cessation tax refund – will become superfluous once a general settlement scheme is introduced, and it is therefore proposed that these be discontinued.

A further proposal is that corporation tax be made deductible from the special tax base. This will ensure good coordination between the taxes and that the cash-flow tax has an entirely neutral effect. The special tax base will be reduced if corporation tax becomes deductible, and a technical increase in the special tax rate to 71.8% will be required to ensure that the total tax rate remains at 78% $(22\% + (1 - 0.22) \times 71.8\% = 78\%)$.

When corporation tax becomes deductible from the special tax base, the corporation tax system will no longer need to include special loss arrangements. Accordingly, it is proposed that the following be eliminated: carrying forward with an interest supplement, the exploration cost tax refund and the cessation tax refund. As of the 2022 tax year, losses will be carried forward net of interest for corporation tax purposes, as in other business sectors.

As part of the transition to the new rules, it is proposed that the tax value of losses and any unutilised uplift under the special tax system, as well as any corporation tax losses carried forward from earlier years, be settled in conjunction with the tax assessment for the 2022 tax year. This will eliminate the need to apply different loss rules in future years. Settling historical losses in connection with the tax assessment for 2022 will give companies an additional liquidity injection.

Overall, the proposal means that companies will cover approximately 22% of their future investment costs. This is close to the companies' proportionate share under an entirely neutral tax arrangement (23%). The difference between the two figures is due to the fact that the depreciation period under the corporation tax rules is shorter than the estimated useful life of the assets.

While the switch to a cash-flow tax will boost the State's revenues in the long term, revenues will drop initially. In 2022, the revenue loss is forecast to total approximately NOK 45 billion, including a revenue reduction of approximately NOK 6 billion linked to settlement of the tax value of historical losses and unutilised uplift. In the longer term, the new system is expected to increase revenues by approximately NOK 7 billion (present value) with respect to investments made in 2022. As the proportion of investments subject to the cash-flow tax rather than the temporary tax rules grows, the revenue effect of the new system will intensify.

In calculating the revenue effect over time, secure investment deductions have been valued using a risk-free rate. Several companies have stated that they apply a significantly higher risk-adjusted required return when valuing secure tax deductions and other cash flows. Whether or not the proposal constitutes a tax hike for companies in respect of new investments depends on the size of the required return these companies apply when valuing future deductions.

Petroleum industry tax receipts form part of the cash flows generated for the State by the petroleum industry, which are transferred to the Government Pension Fund Global (GPFG) in full. The proposed change therefore has no consequences for the 2022 budget, but will affect financial leeway in future budgets through its impact on the GPFG.

The proposal necessitates adjustments to the tax return and the systems used by the tax authorities. During a transitional period, several sets of rules will have to be applied in tandem. Overall, however, the administrative consequences are forecast to be moderate.

The Ministry of Finance requests feedback on the consultation proposal by 3 December 2021. The Ministry anticipates that the necessary statutory changes can be submitted to the Storting in a dedicated draft act in the spring of 2022. The changes will apply to investments made as of the 2022 tax year, with the exception of investments covered by the temporary tax rules in section 11.