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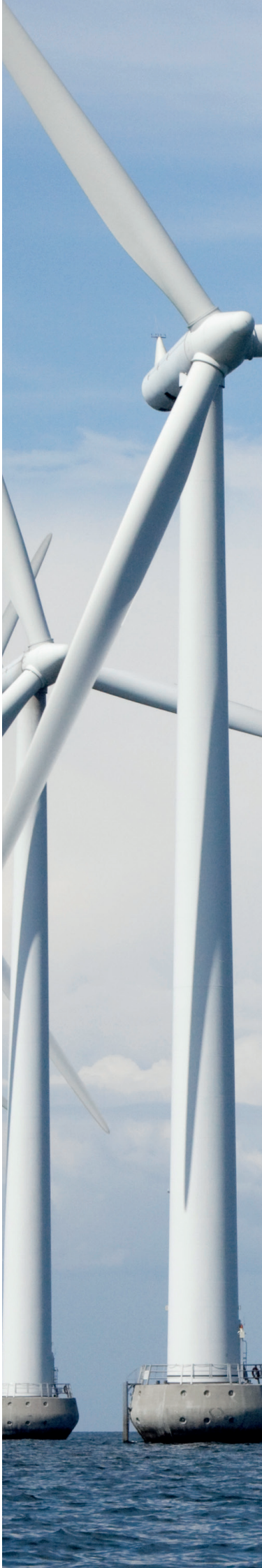
IMPACT OF UKCS FISCAL POLICY ON UK ECONOMIC GROWTH

2025

An analysis of the change in tax receipts, economic value, jobs, and energy security



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IMPACT OF UKCS FISCAL POLICY ON UK ECONOMIC GROWTH 2025

FUTURE UKCS FISCAL POLICY TO SUPPORT UK ECONOMIC GROWTH

A paper to outline the opportunity of fiscal change to deliver long-term economic growth that supports production, investment and jobs.

This paper provides an assessment of the impact of a 2026 implementation of the proposed permanent mechanism to respond to unusually high prices and compares that to a delay in implementation until 2030.

The North Sea is a strategic national asset and has powered the economy and homes for the past 50 years and remains an important strategic asset for the UK. Today, around 75% of the UK energy needs are met by oil and gas, with 50% of this coming from the UK Continental Shelf (UKCS). The UKCS supports a workforce of around 200,000 jobs across from Shetland to Southampton. With the right policy, the North Sea can continue to power the country for decades to come through the responsible production of oil and gas alongside the build-out of renewables and low-carbon technologies.

As currently proposed by HM Treasury (HMT), any fiscal changes would not be in place until post-2030, this is too long a period to wait. Our sector's investment cycle is measured in decades and our members, at the heart of UK plc, are looking to make decisions now that will impact the latter half of the decade and beyond. We need a long-term solution in place now.

The impact of implementing an appropriate price mechanism in 2026 compared to the current post-2030 proposal, coupled with a pragmatic outcome to the ongoing "Building the North Sea" consultation, is:

- Tax receipts in 2030/2031 at the end of the 5-year period are forecast to be over £1 billion higher under the scenario where the permanent mechanism is implemented in 2026 rather than 2030 assuming OBR prices. Total tax receipts in the 2025 to 2050 period increase overall by an estimated 25%.
- Unlock an anticipated increase of around £41 billion of capital investment in the UKCS in the period 2025 to 2050, producing an additional 2.5 billion barrels of oil equivalent over that period.[1] Whereas, a delay to the implementation of the proposed permanent mechanism will result in the sterilisation of the opportunity with the accelerated cessation of production of critical hubs and infrastructure and the loss of critical mass of UK oil and gas supply chain capability.
- An expected increase in total associated economic value of the sector of approximately £42 billion in the period 2025 to 2034, with an increase of approximately £137 billion of total economic value in the period 2025 to 2050.
- Support for an additional 23,000 direct and indirect jobs in the oil and gas sector in 2030 alone due to continued investment in domestic oil and gas production.

[1] https://www.westwoodenergy.com/news/westwood-insight/westwood-insight-ukcs-geological-potential-remains-but-sentiment-shift-is-needed

The Energy Profits Levy (EPL) was introduced in May 2022 and was initially set at 25% until 2025. It was later increased to 35% and extended twice to conclude in 2029. Following the General Election, this was then increased by a further 3% and extended to 2030. The levy is designed to tax exceptional profits from oil and gas production, particularly those arising from high prices, and is currently set to expire in 2030.

The EPL has not delivered the expected tax revenue, with less than 40% of the forecast 2022 tax revenue now expected to be achieved in the period from 2023 to 2028. In November 2022, the OBR forecast that the total expected tax from the UKCS in the period 2023 to 2028 would be £65.7 billion. In March 2025, the OBR forecast that the total tax take for the same period was revised to £21.1 billion. The OBR expected tax yield for the same period has continuously fallen over the last 2 years despite ongoing fiscal change.

In 2024, the UK's total energy production was at a historic low, with over 40% of the UK's energy needs met through imports. Without stimulating investment, the UK will be reliant on imports for over 80% of oil and gas demand by 2030. The Prime Minister and the Chancellor of the Exchequer have spoken this year on the importance of oil and gas production from the North Sea alongside renewable energy as vital for providing energy security. Fatih Birol of the International Energy Agency (IEA) has also stated that further investment in oil and gas is needed alongside an ambitious acceleration of renewable energy for global energy security.

Significant oil and gas reserves remain in the North Sea that can be unlocked to support UK energy security aligned with the UK climate ambitions. With continued support for the sector through existing licences, responsible access to new licences where needed, and a return to a competitive and stable fiscal and regulatory environment the UKCS this number could increase, delivering over half of the UK oil and gas demand in that period.

There is greater opportunity in the North Sea than currently forecasted. Official forecast of the production from the UKCS has declined significantly in the past 5 years from an estimated 6.7 billion barrels of oil equivalent to less than 4 billion barrels in the period 2025 to 2050 with an estimated loss of £160 billion of economic value in the UK over that period. The North Sea Transition Authority (NSTA) currently forecasts the UKCS to produce less than 4 billion barrels of oil and gas equivalent in the period 2025 to 2050, which is less than one-third of the UK demand forecast in the Climate Change Committee balanced pathway to net zero. Over the period 2019 to 2024, the NSTA has reduced expected production volumes from the UKCS. The current forecast for production is reflective of the cumulative effect on the sector of the past 5 years including the impact of COVID-19, uncertainty around future licensing and fiscal uncertainty has undermined investment. There is greater opportunity in the North Sea than currently forecasted.

The Government has committed to ensuring that there is a new permanent mechanism in place to respond to future oil and gas price shocks, recognising the current energy profits levy (EPL) introduced in response to an extraordinary spike in price should be reformed. This new mechanism will form an integral part of the fiscal regime and is intended to begin to rebuild the certainty and confidence that the oil and gas sector needs to see in the future fiscal landscape, to help protect businesses and jobs now and for the future.

Independent data from the Office of National Statistics (ONS) confirms that the profits for those investing in the UK Continental Shelf (Oil and Gas producers) have fallen to levels that do not represent windfall profits. For the last 4 quarters where ONS data is available (Q3 2023 to Q2 2024), the ONS estimates that the rate of return in the basin has been negative with an average rate of return estimated at -1% in that period. Action is required now to address the attractiveness of the UKCS for investment.

Action is required now to remove the EPL and replace it with the proposed permanent mechanism to respond to future price shocks. Without a more immediate response, it is anticipated that the sector will experience an accelerated decline, losing critical supply chain capability, and infrastructure future production opportunities from the UKCS. The industry remains concerned that the risk of capital and activity flight under the current regime will leave the sector without the breadth and depth needed to deliver energy security and the transition, to the detriment of employment across the UK.

PRINCIPLES FOR AN OIL AND GAS PRICE MECHANISM THAT ENSURE THE UK'S ONGOING ECONOMIC, ENERGY SECURITY AND NET-ZERO AIMS

The objective of any fiscal regime is a fundamental decision for any Government, however the decision to implement a reformed EPL mechanism ahead of 2030 will dictate the shape of tax receipts, investment, and activity for decades to come. Successful fiscal regimes that deliver enduring economic value are based on a clear and stable set of principles that give certainty to investors. This stability will in turn reduce the currently elevated cost of capital for North Sea companies which will further encourage additional investment activity.

Taxes should be profit-based. An oil and gas price mechanism should target only the profit derived from unusually high prices rather than the total profit base. This ensures that Government and companies make a competitive return whilst also ensuring the sector can continue to invest. These fundamental factors are in line with the profit-based mechanism proposed in the industry's consultation response.

The definition Government set for unusually high price environment is fundamental to future activity on the UKCS and positioning of the UK as internationally competitive and open for business. This definition should be based on a clear methodology and independent of the rate or mechanism applied to capture rent from these periods.

Defining unusually high prices should be calculated based on a clear methodology, we propose the following principles are embedded to deliver this when setting the threshold:

- **Historic prices should be used** given this is a stronger reference of the market as opposed to forward curves. This also allows for greater clarity around the normal price scenario in the market to be considered and recognise the response to the market given global events and the abnormalities.
- **The period used to set the methodology for both oil and gas prices should be the same** to give a common reference point. Proposed the look back period would consider the last 10 complete calendar years recognising the structural shift in Brent and NBP in recent years.
- **The reference price from historic data should not be an average** but instead an order of magnitude such as 85th percentile as a floor. The threshold must be set at a level that supports positive investment decisions whilst also exceeding normal movements in the market and sustained structural changes.
- **The separate reference point for oil and gas as outlined above should be set and then adjusted annually for inflation,** giving certainty to the market and Government should a high price environment arise.
- **The threshold should be defined by a methodology rather than goal-seeking a specific rate of return.** This would be delivered by the threshold being set at a level which exceed the normal movements in the market, and therefore the underlying cost profile with adjustments.

Following the above methodology and using public available data sets for Brent and NBP 2015 – 2024 inclusive that are adjusted by the March 2025 UK GDP deflater, 85th percentile is $94/barrel and 119p/therm. The methodology above also assumes a profit- based mechanism is used to capture rent from unusually high prices, if a revenue mechanism was introduced and the rate wasn't adjusted this threshold would have to be revised upwards.

CONCLUSIONS

A decision to replace the EPL by 2026 would positively benefit energy security, economic growth, and employment.

The UKCS needs a competitive, progressive, and stable regime that promotes investment. The existing EPL was designed for a short-term price shock that has now disappeared and therefore the levy needs to be reconsidered. Investment across the energy landscape, including to further support the responsible production of oil and gas, will largely be dictated by decisions made around the fiscal and regulatory environment.

The offshore energy supply chain, which will be critical to delivering a homegrown transition, is already being pulled to other regions which offer a more stable and attractive environment. Once the supply chain, infrastructure and skilled people leave, the challenge to get them back comes at an increased cost of doing business for the offshore energy sector in the UK, further risking our energy security and chances of delivering an orderly and just energy transition. Positive decisions to reform the EPL, whilst also giving the Government the certainty that in unusually high prices the mechanism would ensure a

sharing of rent, will help protect the existing UK supply chain and demonstrate that the UK, as a centre for excellence in energy production, is open for business.

A fiscal regime based on clear principles that provide investors with certainty is essential to the delivery of energy security, net zero, and macroeconomic growth. Competition for capital is fierce, and therefore, the attractiveness of the UK on an international scale will be critical.

A mechanism introduced in 2026 targeting the profit earned above the unusually high threshold is a significant lever to deliver both short and long-term economic growth. The UK tax regime must have long-term predictability; full expensing of capital should be maintained with long-term certainty on allowances which are designed to ensure a competitive regime.

A homegrown energy transition will strengthen the UK energy supply chain, accelerate the production of domestically produced energy, and mean no individual, community, or sector is left behind in the UK's journey to net zero.

ADDITIONAL INFORMATION

1. THE ROLE OF DOMESTIC OIL AND GAS PRODUCTION IN THE UK ENERGY MIX

1.1 CURRENT ENERGY MIX

Today, the UK relies on oil and gas for 75% of its total energy needs. The UK domestic oil and gas sector currently provides approximately 50% of that total demand for the UK, with the remainder of the oil and gas needs provided through imports.

In 2024, the UK's total energy production was at a historic low, with over 40% of the UK's energy needs met through imports.[2]

With supportive policy and the right economic environment, the North Sea will continue to power the country through responsible production of oil and gas alongside the build-out of renewable energy. The successful path for the UK is one that recognises the role of both oil and gas plus renewables; and not one versus the other, to deliver an integrated energy system that can respond to the UK's needs. Homegrown energy production must be prioritised over imported energy.

Future UK oil and gas activity is compatible with net-zero and the UK's climate leadership ambitions. Domestic oil and gas production is complimentary to the Government's Clean Power 2030 ambitions and avoids offshoring our emissions and losing skills, supply chain and infrastructure overseas.

Oil and gas produced in the UK have a lower carbon footprint than imported alternatives. By choosing to prioritise domestic production as part of an integrated energy system, rather than importing LNG to meet the demand for gas, this would reduce production emissions by an estimated 58 million tonnes of CO_2 over this period.[3]

[2] Department for Energy Security and Net Zero Energy Trends March 2025

[3] This assessment is made on the basis that incremental gas produced domestically will reduce the requirement for LNG imports produced at a higher carbon intensity. Reference data NSTA Carbon Emissions Intensity Analysis - The North Sea Transition Authority

1.2 UKCS OIL AND GAS PRODUCTION POTENTIAL

At the end of 2023, the North Sea Transition Authority estimated that the total remaining oil and gas reserves and contingent resources in the UKCS totalled 9.4 billion barrels of oil equivalent.

The mean Prospective Resources in mapped Leads and Prospects are estimated as 3.5 billion barrels of oil equivalent. This is supplemented by an additional mean Prospective Resource of 11.2 billion barrels of oil equivalent estimated to reside in Plays outside of mapped Leads and Prospects.

TABLE 1: UKCS RESERVES AND RESOURCES CENTRAL ESTIMATES AS AT END 2023 IN BILLION BARRELS OF OIL EQUIVALENT

		Billion BOE
Reserves (2P)	Proven and Probable	3.3
Contingent Resources (2C)	Total	6.1
	Producing Fields	1.6
	Proposed New Developments	1.5
	Marginal Discoveries	3.0
Prospective Resources	Total	14.7
	Prospects and Leads	3.5
	Plays	11.2
Total Reserves + Contingent Resources		9.4
Total Reserves + Contingent + Prospective Resources		24.1

The total reserves and resources estimated by the North Sea Transition Authority total 24.1 billion barrels of oil equivalent.[4]

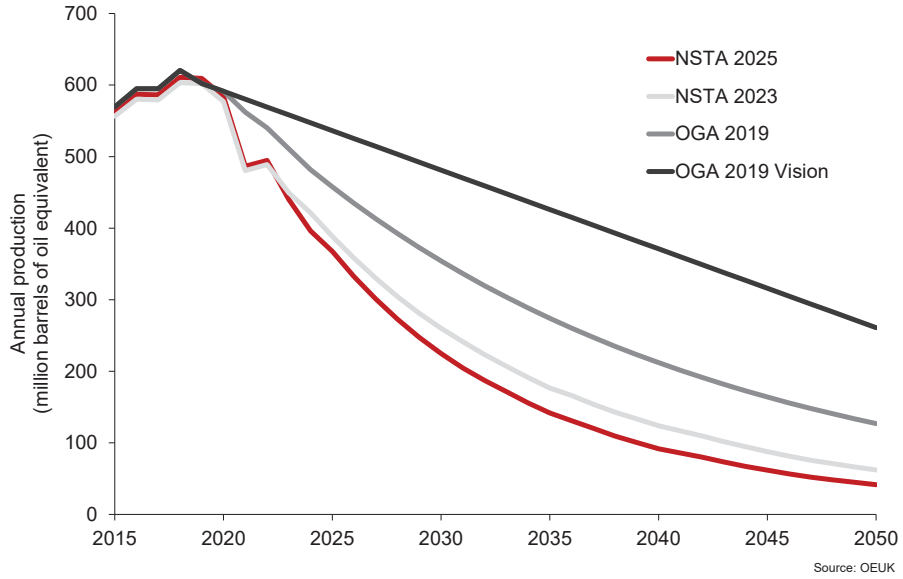
In March 2025, the NSTA forecast that the UK was on track to produce 3.8 billion barrels of oil and gas in the period 2025 to 2050[5]. This represents production of only 15% of the total reserves and resources identified by the NSTA in the basin.

The North Sea Transition Authority has consistently reduced expected production volumes from the UKCS in the period 2019 to 2024.

[4] NSTA 2024 UK Oil and Gas Reserves and Resources Report at the end of 2023

[5] NSTA March 2025 Data and insights - Production and expenditure projections

Figure 1 - North Sea Transition Authority Production Estimates 2019 to 2025



In 2019, the OGA (renamed as the North Sea Transition Authority in 2022), forecast total production in the UKCS of 6.7 billion barrels of oil equivalent in the period 2025 to 2050 period[6]. The OGA also provided a 2019 Vision in which with supportive policy the UKCS produced a total of 10.4 billion barrels of oil equivalent in that period. These forecasts were based on the positive increases in forecast reserves achieved in the period following 2016 when the UKCS tax was aligned to promote investment and the recommendations of the Wood Review implemented.

TABLE 2: UKCS LOSS OF ECONOMIC VALUE SINCE 2019

Production Estimate	NSTA 2025	NSTA 2023	OGA 2019	OGA 2019 Vision
Total Production 2025 to 2050 Billion Barrels of Oil Equivalent	3.8	4.5	6.7	10.4
Loss of Economic Value 2025 to 2050 (GVA) £Billion (reference to 2019 OGA estimate)	-£160	-£120	-	+£200

[6] NSTA March 2019 Projections of UK Oil and Gas Production and Expenditure

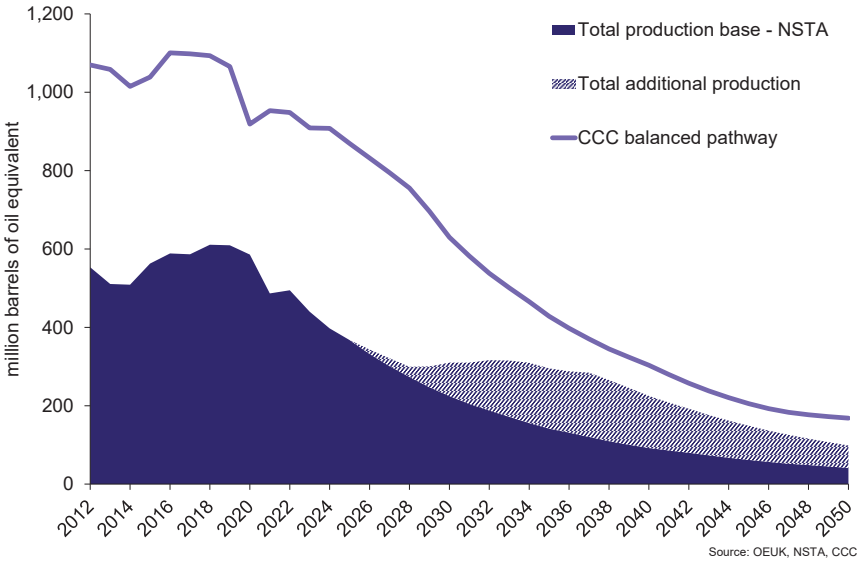
In 2023, the forecast total production in the UKCS was reduced to 4.5 billion barrels of oil equivalent in the period 2025 to 2050, and in 2025 further reduced to 3.8 billion barrels of oil equivalent. The 2025 NSTA forecast for production is reflective of the cumulative effect on the sector of the past 5 years including the impact of COVID-19, uncertainty around licensing, fiscal policy decisions including the implementation of EPL and subsequent changes to the regime, and regulatory uncertainty that have undermined investment. The underlying UKCS geology remains the same but expected outcomes have been impacted by COVID-19 and subsequent policy decisions.

The 2025 NSTA estimate of total production in the period 2025 to 2050 represents a loss of economic value of £160 billion in that period compared to the 2019 OGA forecast, and a loss of £360 billion of economic value in that period compared to the OGA 2019 Vision.

1.3 ROLE OF OIL AND GAS ON THE UK JOURNEY TO NET ZERO

The Climate Change Committee (CCC) estimate the UK will require circa 11 billion barrels of oil equivalent (boe) in the period 2025 to 2050 to meet its energy needs[7]. The NSTA currently forecast the UK to produce around a third of the CCC balanced pathway forecast demand. In the right economic environment and policy environment including access to new licences where needed, and a competitive fiscal and regulatory environment

Figure 2: UKCS Production Projects compared with Climate Change Committee (CCC) balanced pathway



the UKCS could sanction a further 2.5 billion barrels of oil equivalent in the period 2025-2050.

This would mean the UKCS could support half of the UK demand and add significant gross value to the UK economy whilst maintaining support for the current workforce. Oil and gas produced in the UK has a lower carbon footprint than imported alternatives. By choosing to prioritise domestic production as part of an integrated energy system, rather than importing LNG to meet the demand for gas, this would reduce production emissions by an estimated 58 million tonnes of CO_2 over this period.

[7] https://www.theccc.org.uk/publication/the-seventh-carbon-budget/

1.4 MAXIMISING ECONOMIC RECOVERY AND NET ZERO

In 2014, Sir Ian Wood published a review targeted at arresting the decline in oil and gas production from the UKCS[8]. The review resulted in the formation of the Oil and Gas Authority (subsequently the North Sea Transition Authority).

In December 2014, the Treasury issued a review of the fiscal regime necessary to maintain investment as the basin matures. This resulted in the reduction in the headline rate of tax for the UKCS to 40%[9].

In the period from 2015 to 2019, because of supportive policy, production from the UKCS was effectively flat with an average of 600 million barrels of oil equivalent produced annually.

Since 2020, the impact of COVID-19, fiscal policy decisions including the implementation of EPL and subsequent changes to the regime, and regulatory uncertainty that have undermined investment. As a result, the decline rate from the basin in the period 2020 to 2024 has accelerated to 9% per annum. This decline can be arrested with supportive policy.

2. UKCS FISCAL MODEL

A financial model has been used to determine the impact of the implementation of a change to the UKCS fiscal regime to remove the EPL and replace it with an appropriate permanent mechanism to respond to future price shocks. The output of the model gives a prediction of the potential for energy security, jobs, capital investments and return to HMT in the right investment, economic, and policy environment.

2.1 FISCAL MODEL ASSUMPTIONS -

- The 2030 model assumes that a profit-based permanent mechanism is introduced in 2030. The production profiles associated with the base case are aligned with the NSTA's 2025 production forecast. Under this scenario, total production from the basin falls approximately 40% from 2025 to 2030, with a resultant acceleration of the cessation of production of key offshore hubs. Total production amounts to 3.6 billion barrels of oil equivalent in the period 2025 to 2050.
- The 2026 model assumes that a profit-based permanent mechanism is introduced in 2026. The production profiles associated with the upside case are aligned with the NSTA's 2025 production forecast with additional projects unlocked. Under this scenario additional capital investment results in a significantly shallower decline in production with a total production reduction of 15% from 2025 to 2050. With the managed decline additional investment opportunities are unlocked post 2030. Total production amounts to 6.1 billion barrels of oil equivalent in the period 2025 to 2050.
- The modelling assumes that, in both the 2026 and 2030 cases, full capital relief is available.

[8] Sir Ian Wood 2014 UKCS Maximising Recovery Review FINAL 72pp locked.pdf

[9] Driving Investment 2014 Driving investment: a plan to reform the oil and gas fiscal regime

2.2 FISCAL MODEL PARAMETERS

- The model is run on two separate price profiles; (1) OBR March 2025 forecast (2) the price curve seen in oil from 2006 and the recent NBP prices replicated from 2025 onwards reflecting a high price environment. The model assumes a constant £:$ exchange rate of 1.3.
- The model assumes a profit-based mechanism is introduced at oil and gas threshold prices of $94/bbl and 119p/therm respectively (85th percentile of real- term prices in the last 10 years). The model assumes that the additional tax is levied at 38%, resulting in a headline rate of tax of 78% for profits above the oil and gas price thresholds.
- Total economic value (GVA) is calculated based on a direct and indirect multiplier derived from production 2019-2022. The multiplier is used on the production profile. The methodology is consistent with previous assessments.[10]
- The total jobs in the sector is calculated based on a direct, indirect and induced jobs multiplier derived from production in the period 2019-2022.
- The modelling assumes that, in both the 2026 and 2030 cases, full capital relief is available.
- The model used in this paper does not consider losses in the period.

2.3 FISCAL SCENARIOS

The following scenarios are presented to present the opportunity of an earlier removal of EPL and implementation of a reformed mechanism to capture rent from unusually high prices.

For the purposes of this modelling, unusually high prices are defined as those that exceed $94/bbl and 119p/therm. The mechanism captures the difference in rent between the threshold and the average market price for this period.

This is the currently proposed PBM mechanism in the oil and gas price mechanism consultation however further consideration. We have not modelled this on realised prices however note this should be considered further.

Scenario 1: 2030 Model EPL expiring in 2030 and a successor introduced.

- Headline tax rate at 78% and a maximum relief of 84.25p/£ until 2030, successor mechanism introduced that if oil and gas prices both exceed the threshold at most has a 38% and 38/£ split with profits apportioned to oil and gas.
- The 2030 model assumes that a profit-based permanent mechanism is introduced in 2030. The production profiles associated with the base case are aligned with the NSTA's 2025 production forecast. Under this scenario, total production from the basin falls approximately 40% from 2025 to 2030, with a resultant acceleration of the cessation of production of a key offshore hubs. Total production amounts to 3.6 billion barrels of oil equivalent in the period 2025 to 2050.

[10] Impact of UKCS Fiscal Policy on UK Economic Growth - Autumn 2024 Analysis | Offshore Energies UK (OEUK)

Scenario 2: 2026 Model EPL removed in 2026 and a successor introduced.

- Headline tax rate at 78% and a maximum relief of 84.25p/£ until YE 2025, successor mechanism introduced that if oil and gas prices both exceed the threshold at most has a 38% and 38/£ split with profits apportioned to oil and gas.
- The 2026 model assumes that a profit-based permanent mechanism is introduced in 2026. The production profiles associated with the upside case are aligned with the NSTA's 2025 production forecast with additional projects unlocked. Under this scenario additional capital investment results in a significantly shallower decline in production with a total production reduction of 15% from 2025 to 2050. With the managed decline additional investment opportunities are unlocked post 2030. Total production amounts to 6.1 billion barrels of oil equivalent in the period 2025 to 2050.

TABLE 3: FISCAL SCENARIOS OUTPUTS

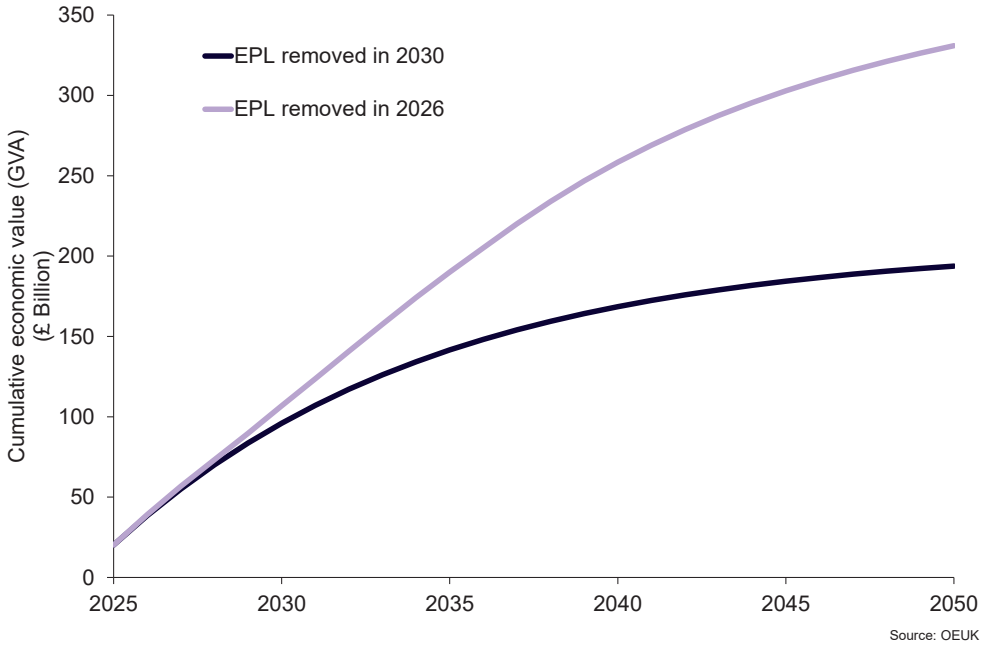
		10 year period 2025 to 2034					Total 2025 to 2050			
Scenarios	Prices	Capital Investment (£Billion)	Additional Production (boe)	Total RF tax take (£Billion)	Additional GVA (£Billion)	Additional direct + indirect jobs supported in 2029	Capital Investment (£Billion)	Additional Production (boe)	Total RF tax take (£Billion)	Additional GVA (£Billion)
Scenario 1: EPL removed in 2026 and a successor introduced	OBR Price-Deck	36.5	3.2	36	174	93,000	66.2	6.01	63.2	£331
Scenario 2: EPL expiring in 2030 and a successor introduced	OBR Price-Deck	21.2	2.4	42	132	70,000	24.9	3.52	51.2	£194

		10 year period 2025 to 2034					Total 2025 to 2050			
Comparison Scenarios 1 & 2	Prices	Capital Investment (£Billion)	Additional Production (boe)	Total RF tax take (£Billion)	Additional GVA (£Billion)	Additional direct + indirect jobs supported in 2029	Capital Investment (£Billion)	Additional Production (boe)	Total RF tax take (£Billion)	Additional GVA (£Billion)
Scenario 1 Scenario 2	OBR Price-Deck	15.3	0.76	-5.8	41.8	23,000	41.3	2.49	12	136.95

Implementing an appropriate price mechanism in 2026 compared to the current post-2030 proposal could result in:

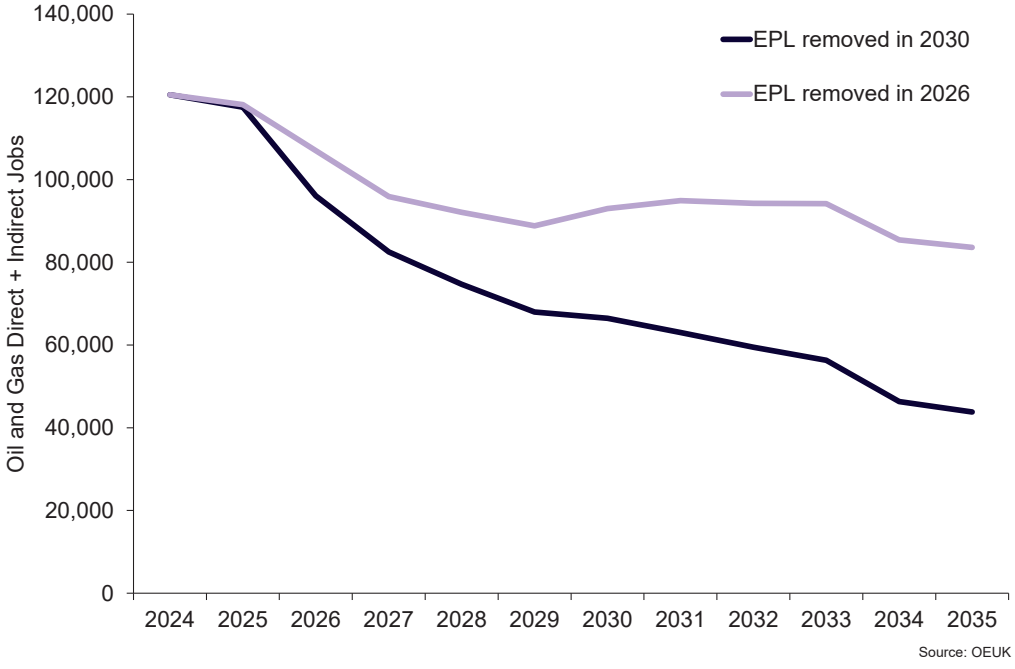
- Tax receipts at the end of the 5-year period, in 2030/2031 are forecast to be over £1 billion higher under the scenario where the permanent mechanism is implemented in 2026 rather than 2030 assuming OBR prices. Total tax receipts in the 2025 to 2050 period increase overall by an estimated 25%.
- The production of an additional 2.5 billion barrels of oil equivalent of additional production potentially being unlocked through an anticipated increase of around £41 billion of capital investment in the UKCS in the period 2025 to 2050. A delay in the implementation of the permanent mechanism will result in the sterilisation of the opportunity with the accelerated cessation of production of critical hubs and infrastructure and the loss of critical mass of UK oil and gas supply chain capability.
- An expected increase in the total associated economic value of the sector of approximately £42 billion in the period 2025 to 2034, with an increase of approximately £137 billion of total economic value in the period 2025 to 2050.
- Support for an additional 23,000 direct and indirect jobs in the oil and gas sector in 2030 alone due to continued investment in domestic oil and gas production.

Figure 3: Comparison of Economic Value (GVA) under proposed scenarios



In the event that the EPL is replaced in 2026 with a permanent mechanism, the total economic value associated with the additional production totals £331 billion in the period 2025 to 2030. Under the scenario where EPL is not removed until 2030, the total economic value is £194 billion in the same period. Incentivising investment in the sector results in additional economic value of £137 billion in the period 2025 to 2050.

Figure 4: Comparison of direct and indirect job retention under proposed scenarios



3. OIL AND GAS PRICE ENVIRONMENT

Oil prices are lagging indicators and can be influenced by a number of factors including geopolitical decisions and global supply/demand tensions. Originally the UK were price setters, however, structural changes over decades including a change in production output and an increase in imported energy mean the UK has become price takers in a global market. Brent is priced globally, and history shows the influence of weakening in the global economy, invasions and changes to production in countries such as the Middle East and the United States. Brent and NBP are independent markets – this is a trend which has only increased in recent years as NBP further diverged from Brent.

Whilst oil prices continue to be set on the global market, underlying operating costs are more heavily influenced by the domestic market and access to supply chain. The impact of the illegal Ukraine invasion and broader disruption to trade routes have impacted the costs within the supply chain which in the face of an ever-decreasing oil price has a significant impact on the overall viability of projects.

Figure 5: Annotated brent graph showing impact of events on the market

Source: OEUK

The unusually high gas prices seen in 2022 were largely driven by the rebound in activity post COVID-19, the invasion of Ukraine changing the production profile for European gas and the peak LNG imports from the US to meet UK demand in the year. Prior to 2022, we began to see a step change in the normal prices we see in the NBP market however this has been further cemented. This structural change is irreversible considering UK production profiles and expected changes in demand. There continues to be an increasing likeness between NBP and markets like Japanese Korea Marker (JKM) which too is heavily reliant on imported products.

Therefore, when setting the methodology to derive unusually high prices, this context must be closely considered. The oil and gas markets are distinctively diverse and influenced more acutely by different factors. This is evident in the price trends seen over the last 10 years and the new norms in both markets. The robustness of the future oil and gas price mechanism will be underpinned by the clarity around the methodology which determines the high price scenario. There is a clear trend in prices when looking at this historically which should allow a specific "unusually high price" to be derived.

Figure 6: Real Brent frequency 2015-2024

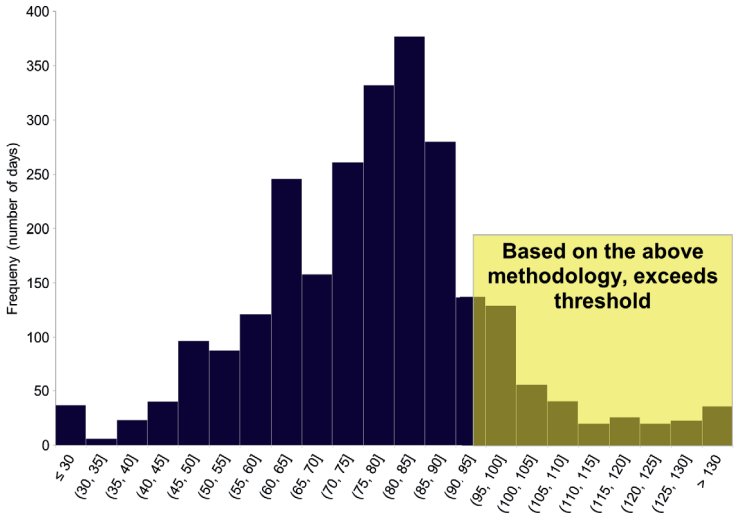
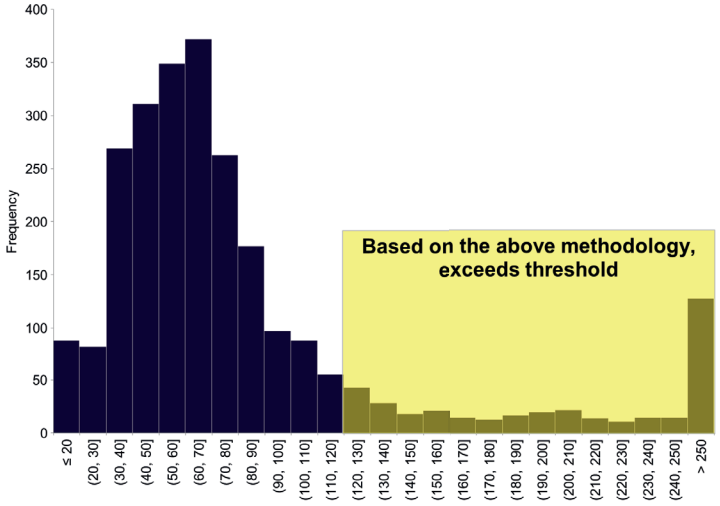


Figure 7: Real NBP Price frequency 2015-2024



4. PROFITABILITY OF THE UK CONTINENTAL SHELF

The windfall tax for both oil and gas producers and electricity generators was introduced on the basis of windfall profits made by the organisations associated with these activities.

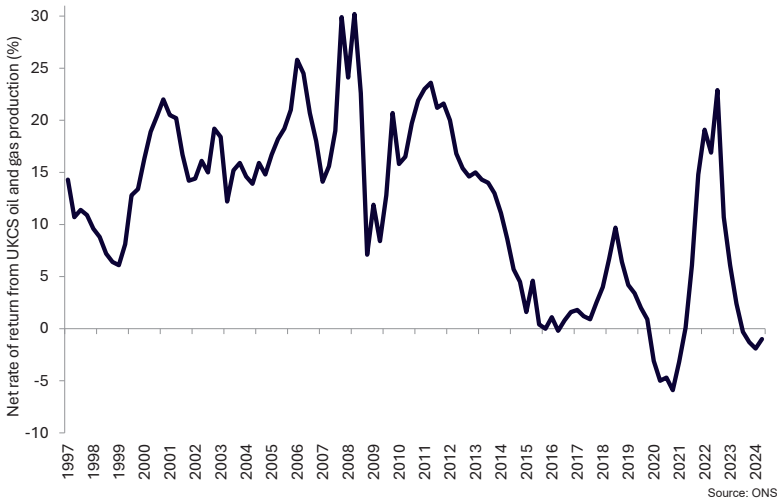
As commodity prices have returned to align with long-term real-term averages, profits made in both oil and gas and energy generation have reduced. In 2023, the Government recognised this by removing the electricity generator levy on electricity-generating companies.

Independent data from the Office of National Statistics (ONS) indicates the profits for those investing in the UK Continental Shelf (Oil and Gas producers) have fallen to levels that are not considered to be windfall profits and are significantly below other areas of the UK economy.

For the last 4 quarters where ONS data is available (Q3 2023 to Q2 2024), the ONS estimates that the rate of return in the basin has been negative with an average rate of return estimated at -1.1% in that period.

There has been a further softening of commodity prices in 2025.

Figure 8: Office of National Statistics UKCS Rate of Return



5. OFFICE OF BUDGET RESPONSIBILITY (OBR FORECAST)

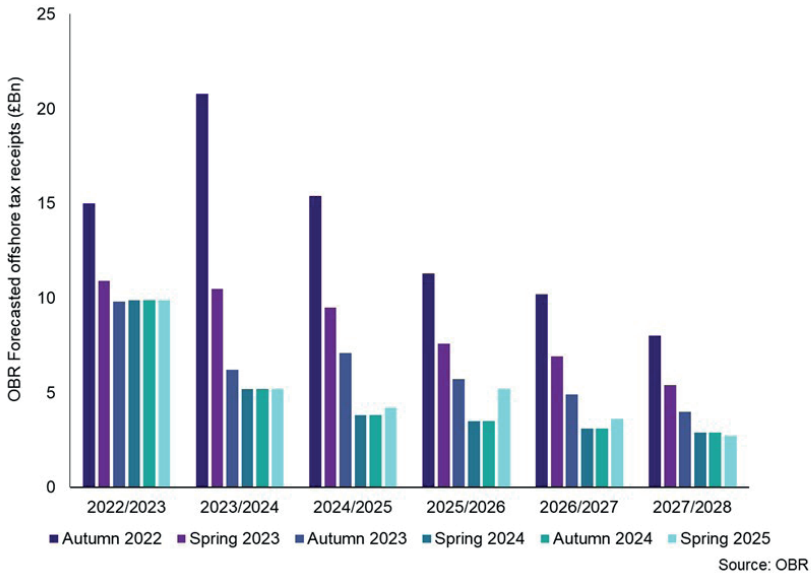
The Office of Budget Responsibility provides a forecast of the total tax payments from the UKCS (corporation tax, energy profits levy, net of production revenue tax).

The OBR total tax payment forecasts have been revised downwards at each fiscal moment as both commodity prices have reduced and the forecast production volumes from the basin have reduced.

In November 2022, the OBR forecast that the total expected tax from the UKCS in the period 2023 to 2028 would be £65.7 billion. In March 2025, the OBR forecast that the total tax take for the same period was revised to £21.1 billion. The OBR expected tax yield for the same period has continuously fallen over the last 2 years despite ongoing fiscal change with now less than 40% forecasted.

The modelling conducted to support this paper predicts a higher tax take from the UKCS than those forecast by the Office for Budget Responsibility. The OBR modelling is based on the input production data from the NSTA and average prices for a fixed period. The OBR model is also rationalised against HMRC actual payments on a delay; this model does not reflect losses.

Figure 9: OBR forecast of UKCS tax receipts. The OBR forecast has been revised down at each fiscal moment



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