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Oil and gas taxation in Norway

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1.0 Summary

The Norwegian Oil and Gas Taxation Code includes direct and indirect taxation. Direct taxation plays the most important role for companies investing in upstream activities on the Norwegian continental shelf. This summary on Norway relates to exploration and production activities on the Norwegian Continental Shelf ("NCS"), as there are no onshore activities in Norway.

In order to explore and produce petroleum resources on the NCS, a licence is needed from the Ministry of Petroleum and Energy ("MPE").

The petroleum activities on the NCS are governed by The Law on Petroleum Activities dated 29 November 1996, which provides extensive rules in respect of rights and obligations for licensees.

The Norwegian petroleum tax system is based on the taxation of the entity rather than taxation of specific petroleum assets.

Direct taxes consist of:

- ordinary petroleum tax 27%
- special tax 51%

Losses, as a rule, may be carried forward indefinitely. The tax value of exploration costs (78%) may be refunded from the Norwegian state annually. Moreover, the tax value of unused losses when finally ceasing exploration/production activities on the NCS will be refunded by the Norwegian state.

Indirect taxes include carbon dioxide taxes and nitrogen oxide tax. VAT, which generally is the main indirect tax in Norway, plays a limited role for companies engaged in exploration/production on the NCS as supplies to be used in upstream activities are zero rated.

2.0 Corporate income tax

The taxation of upstream activities on the NCS is regulated by the Petroleum Tax Act ("PTA") dated 13 June 1975 and annual decisions made by the Norwegian parliament (regarding tax rates).

The PTA sets out the specific rules for the taxation of upstream petroleum activities. If there are no specific rules covering the particular situation in the PTA, the rules contained in the General Tax Act ("GTA") will apply.

There are, however, important differences between the rules stated in the PTA and the GTA. In this guide we have highlighted the rules stated in the PTA only, unless there are any relevant areas specified elsewhere. We have not commented on tax issues which are relevant for other activities – such as oil service activities on the NCS (such activities are essentially only regulated by the rules in the GTA).

It should be noted that costs may be deductible against income taxable under the PTA even if the costs are actually incurred onshore Norway or elsewhere, provided that the costs relate to taxable activities in accordance with the PTA. This will typically be relevant with respect to administrative costs, but may also for instance apply to tax depreciation of assets located onshore.

Where a company also performs activities that are taxable in accordance with the GTA (where the tax rate is 27%), any costs incurred should be allocated between the different taxable activities according to the GTA and the PTA as if the upstream activities were conducted by a separate and independent legal entity (i.e. based on the arm's length principle).

Upstream petroleum companies in Norway are subject to both ordinary petroleum tax at the rate of 27% and an additional special tax of 51%.

It should be noted that these taxes are calculated independently of each other. A deduction for the special tax paid is not allowed against the taxable income for ordinary petroleum tax and vice versa.

As a starting point, the basis for these taxes is similar. There are however two differences. These relate to:

- interest costs and other financial items; and

- additional depreciation (uplift) allowance when calculating the taxable income for special tax purposes.

Norway does not operate a ring fencing system between different licences and fields on the NCS. However, for companies engaged in business activities other than upstream activities on the NCS, there are limitations as to what extent losses from onshore activities may be off-set against profits taxable according to the GTA (often referred to as "onshore profits" below).

Moreover, the ordinary tax consolidation system in Norway between Norwegian group companies/branches of companies located in the EEA by way of group contributions, does not apply to upstream activities on the Norwegian continental shelf.

2.1 Rates

The rate of ordinary petroleum tax is 27% for profits taxable according to the PTA. The special tax is charged at 51% as an additional tax on these same profits. The rate of ordinary corporation tax is 27%, for profits taxable according to the GTA.

2.2 Taxable income

Taxable income is gross income minus deductions.

For the purpose of calculating ordinary petroleum tax and special tax, gross income includes revenues from production on the NCS as well as substitutes for such revenues, but not financial income such as interest receivable or gains on derivative agreements, even if such income is clearly linked to the production activities. Financial income is taxable according to the GTA only (as "onshore income").

Costs incurred in order to obtain income of a taxable nature are deductible (limitations apply, for example with respect to entertainment expenses).

Costs are generally deductible when the tax payer has an unconditional obligation to pay these costs to another party.

2.3 Revenue

The PTA requires that when calculating taxable income, all petroleum transactions are recorded using a "norm price". This norm price is applied regardless of whether the transactions are between related or unrelated parties.

Consequently, a company will have different revenue figures for tax and accounting purposes. This difference is treated as a permanent difference.

The petroleum price board fixes norm prices in arrears, normally each quarter. In recent years, with frequent oil price changes, the board has fixed monthly norm prices for crude oil. Contractual prices provide the basis for calculating the tax for dry gas. So far norm prices have only been set for propane.

The norm price must correspond to the price at which petroleum could have been traded between independent parties in a free market. The norm price is fixed on a discretionary basis after an overall evaluation of market conditions, taking several types of transactions, reference markets and methods of evaluation into account.

2.4 Deductions and allowances

Costs incurred in order to obtain income of a taxable nature (revenue from the sale of oil and gas) are deductible (limitations apply for example with respect to entertainment expenses).

It should be noted that costs may be deductible against income taxable according to the PTA even if the costs are actually incurred onshore in Norway or elsewhere as long as the costs relate to taxable activities in accordance with the PTA. This will typically be relevant with respect to administrative costs, but may also for instance apply for tax depreciation of assets located onshore.

Exploration costs

All exploration costs are, as a starting point, deductible and may be off-set against profits from production.

Moreover, companies may claim an annual cash refund of the tax value of direct and indirect exploration costs under ordinary petroleum tax and special tax (this amounts to 78% of such costs), with the exception of finance costs, with the amount of the refund limited to the tax value of the net tax losses. This is an alternative to carrying the losses forward.

Abandonment costs

Abandonment costs are deductible when the costs are actually incurred. Accounting provisions made in order to meet future abandonment costs are not deductible.

Capital allowances (depreciations)

When calculating the taxable income both for ordinary petroleum and special tax purposes, capital allowances are available.

Capital allowances for investments made in productions facilities and pipelines and installations which are part of such production facilities and pipelines are calculated on a straight line basis over six years at a rate of 16.66% per year from the date the capital expenditure was incurred. The capital allowances are granted both when calculating the basis for ordinary petroleum tax and special tax.

For special tax purposes, an additional and accelerated capital allowance is granted on capital expenditure. Such additional depreciation is spread over four years. The uplift depends on whether costs are incurred before 5 May 2013.

Costs incurred before 5 May 2013 are subject to an annual uplift of 7.5% – i.e. in total 30%.

For costs incurred after 4 May 2013, the annual uplift is 5.5% (subject to transitional rules), making the total uplift 22%.

The following transitional rules apply:

- for development costs covered by a plan for development and operations ("PDO") or a plan for installation and operations ("PIO") received by the MPE before 5 May 2013, the reduced uplift applies only to costs incurred in the years following the year in which production commences. Moreover, if a PIO or PDO filed after 4 May 2013 is necessary in order to implement a PDO or PIO filed before 5 May 2013 ("connected plan"), the 7.5 % annual uplift will also apply to costs incurred with respect to the plan filed after 4 May 2013 provided that there has not been production before 5 May when the connected plan is filed;

- for development costs incurred subsequent to an application not to prepare a PDO or PIO received by the MPE before 5 May 2013, the reduced rate applies only to costs incurred in the years following the production beginning;

- for development costs incurred subsequent to a notification (and subsequent approval) received by the MPE before 5 May 2013 to the effect that that there will be significant deviations from a previously filed PDO or PIO, the reduced rate applies only to costs incurred in the years following the year production commences; and

- insofar as the applications /notifications regarding PDOs mentioned above relate to an additional investment in a production licence, the 7.5% annual uplift applies to costs incurred up to and including the year the additional investment starts producing.

The transitional rules will (under all circumstances) not have effect for costs incurred after 2020. In certain cases, the Norwegian petroleum tax system applies outside Norway and the NCS in areas where Norway does not have any (other) legislative power, and where any PDO or PIO thus will not be filed with the MPE. This, for example, is the case with respect to the gas transportation system Gassled (involving the UK, Germany, Belgium and France). In case a PIO or PDO would have been needed by the MPE had the investments been made in Norway or the NCS, the same transitional rules as mentioned above will apply.

Unused uplift (which is relevant in cases where the basis for corporation tax is less than the uplift for the year in question) may be carried forward. An annual interest is added to the unused uplift. This rate is fixed year by year by the Ministry of Finance ("MOF").

If production from a field is abandoned, any undepreciated capital costs subject to straight line depreciation, including uplift not utilized, may be deducted in the last year of production.

Other capital investments (office equipment, cars etc.) are subject to tax depreciation on a declining balance at rates from 0-30% per year. Exploration rigs are, for example, depreciated according to the declining balance method at a maximum rate of 14% per annum.

Financing costs

As a starting point, interest and other finance costs accrued are deductible costs for tax purposes provided the terms are regarded to be on an arm's length basis.

There are however certain limitations which effectively have an impact on the deductibility for finance costs with regards to special tax purposes only.

The limitations relate to the "net finance cost", which are interest costs accrued plus currency losses less currency gains on interest bearing debt. Whether or not the debt is intra group is not relevant. (Note that interest receivable is not included in the base).

The maximum deductible net financial cost to be allocated to upstream activities will be fixed as follows:

$$\text{Total actual net financial costs accrued} \times \frac{\text{50\% of the tax value of "relevant assets"}}{\text{Average total interest bearing debt during the year}}$$

The term "relevant assets" includes the following:

- production facilities/pipelines;
- other fixed assets in relation to the upstream activity;
- capitalised R&D in relation to the upstream activity; and
- other intangibles in relation to the upstream activities.

The part of accrued net financial costs which cannot be deducted against (future) profits from upstream activities will initially only be deductible against income from other activities than upstream activities (i.e. activities taxed under the GTA at the rate of 27%) below referred to as "onshore" income.

Interest receivable, currency gains on items other than interest bearing debt and other financial items will initially always be taxable under the GTA. This means that net positive financial items are usually only subject to the 27% corporate tax rate. The only situation where a positive net financial item is subject to special tax is if a net currency gain on interest bearing debt exceeds the interest cost on such debt.

If the net financial items that are initially allocated onshore are negative (after the deduction against profits from ordinary onshore activities), the amount will be retransferred "offshore" but only against the basis for the 27% ordinary petroleum tax; not the 51% special tax. The net losses transferred can be carried forward with interest (as other losses from upstream activities). Further details are provided below.

Example

If, for example, the tax value of qualifying assets (cost less tax depreciation) at the end of a given year is 500, the average interest bearing debt during the year was 700 and that the net financial items as defined was 35, the following deduction would be granted:

35 x 0.5 x 500/700 = 12.5.

The part of the net financial items which are (initially) not deductible based on the formula, is then off-set against income (profits) subject to "onshore" tax (typically net positive financial income other than items included in "net financial items" as defined above). Insofar as this leads to an "onshore" loss (which normally is the case), the remainder is retransferred as a deduction against the basis for ordinary petroleum taxes – but not against the basis for special tax.

If, for example, there was a hedging gain, interest receivable and a currency gain on a receivable (which is subject to onshore taxation only) totalling 8. The part of the "net financial items" not deductible according to the formula (35 – 12.5 = 22.5) would be off-set against the "onshore" profits of 8 and the remainder, 4.5, would be retransferred as a deduction against the basis for (future) ordinary petroleum tax – but not against the basis for (future) special tax.

2.5 Losses

Loss carry forward

Under Norwegian law, tax losses cannot generally be carried back against earlier years' profits.

There is no restriction on the carry forward of petroleum tax losses. Norway does not have any "integrity" measures such as "same business" or "same trade" tests which need to be satisfied in the event of a change of the ownership of a company.

Interest is added to the losses carried forward. The rate is fixed by the MOF annually.

In circumstances where a company disposes of its total Norwegian upstream activities, the purchaser may take over any unused tax losses (i.e. in connection with an asset deal) in relation to the upstream activities if the seller does not claim a refund of the tax value of unused losses. See Section 5 for further details.

Refund of the tax value of losses

As mentioned above, a licensee may claim a refund of the tax value of exploration costs incurred as an alternative to carrying the losses forward. Such costs include all direct and indirect costs incurred in connection with exploration, except finance costs. If the licensee is also involved with production activities on the NCS and has taxable profits from these activities, the refund cannot exceed the tax value of the net tax losses from the upstream activities. The tax value is 78% of the costs / net loss incurred (costs incurred in connection with the development of a field are not included).

The tax value (78%) of any unused losses at the point when a company abandons its Norwegian offshore activities will be refunded by the Government up to the tax value of those losses (in the event that they are not taken over by a purchaser).

As an alternative, it can be carried back two years if a company ceases conducting upstream activities (in the event that they are not taken over by a purchaser).

Losses fixed according to the GTA ("onshore losses")

50% of the onshore losses may be off-set against the basis for ordinary petroleum tax.

No part of onshore losses may be set against the basis for special tax.

The part of the losses that cannot be offset against the basis for petroleum tax may be carried forward indefinitely (against future "onshore income").

2.6 Foreign entity taxation

There are no specific rules pertaining to how the basis for ordinary petroleum tax and special tax are fixed for foreign entities versus Norwegian entities.

It should be noted that whilst generally production licences are only granted to Norwegian companies, companies resident in another European Economic Area ("EEA") country may also qualify.

Pass through agreements may allow a non-Norwegian group company to perform the activities on behalf of the Norwegian licensee (which implies that the non-Norwegian company is taxed accordingly).

3.0 Tax incentives

As mentioned above, licensees may claim:

- an annual cash refund of the tax value (78%) of exploration costs incurred insofar as these costs do not exceed losses; and
- a cash refund of the tax value (78%) of any unused losses at the point when a company abandons its upstream activities on the NCS.

4.0 Payments to related parties

4.1 Transfer pricing

There are no specific transfer pricing rules that apply to upstream activities on the NCS. The ordinary Norwegian transfer pricing rules apply, which are based on the OECD's Transfer Pricing Guidelines.

It should be noted that as the tax rate for companies engaged in upstream activities is 78%, transfer pricing disputes with the tax authority involved (the Oil Taxation Office) are common.

4.2 Thin capitalization

As mentioned in Section 2.4, there are specific limitations as regards deductions of financing costs against the basis for special tax. These rules apply regardless of whether the financing is from a related party or not.

In addition, debt financing from a related party should not exceed what an unrelated party would offer on a standalone basis (i.e. without any group guarantees or the like).

4.3 Interest deductibility

See Sections 2.4, 4.1 and 4.2 above.

5.0 Transactions

Gains on sale of shares are non-taxable for vendors, both resident and non-resident.

As a starting point, capital gains/capital losses arising from the transfer of assets located on the NCS are taxable/deductible. The gains/losses are taken to income and deducted gradually at a rate of 16.67% per year. An uplift is also added, or a deduction taken from the base when calculating the basis for special tax.

However, in practice, most asset deals are exempt from tax based on provisions in section 10 of the PTA. According to section 10, an approval from the MOF is required with regard to the tax effects of a transfer of assets that are under the petroleum tax regime provided that consent to the transfer is needed from the MPE. Consent from the MPE is needed upon a direct or indirect transfer of a licence and where the assets will follow the transfer of the licence. This is applicable if all fixed offshore installations pertaining to a licence are transferred (even if the licence as such is not transferred).

According to regulations adopted based on the section 10 of PTA, capital gains arising from the transfer of assets that are allocated to the petroleum tax regime are not taxable and losses non-deductible (neither when calculating ordinary petroleum tax nor special tax). Moreover, the buyer will take over the seller's tax balances (including the basis for uplift) and other tax positions and stand in the shoes of the vendor.

There are also specific provisions in the regulations dealing with transfers where one of the parties covers future explorations costs, or where the seller covers future abandonment costs pertaining to the assigned interest. Broadly, the regulations state that it will be the party who will eventually bear the costs that may deduct those costs and claim a refund of the tax values of those costs when they accrue (i.e. according to the same system that would apply to the seller if the licence was kept).

It may be possible to ask the MOF for an alternative treatment, for example that the seller shall keep the tax balances, although taxpayers are rarely successful in requesting a step up of the tax values (against which the seller is taxed on a gain).

If the buyer is incorporated during the year of acquisition, the regulations may not be applied and a separate ruling request may be required (often referred to as a "section 10 ruling").

The rationale for the above rules is that the Norwegian state's tax revenues from upstream activities should be unaffected by a transfer.

The rules also apply in the case of an exchange of part licences.

Where there is an adjustment and reallocation of interests in petroleum deposits which are covered by certain production licences, there is a separate set of regulations applicable which also aim to achieve tax neutrality. Broadly, the regulations imply that adjustments shall be made as if the new allocation of interests had been in place from the outset.

As mentioned above, consent from the MOF is also required for an indirect transfer such as a share deal implying a change of control. Such deals are, in practice, straightforward from a tax perspective as there are no withholding taxes regardless of where the shareholder is a resident. Thus, there should not be anything to "neutralise" in the first place.

6.0 Withholding taxes

6.1 Dividends

No withholding taxes are levied on dividend distributions from Norwegian companies with respect to upstream petroleum activities to a corporate shareholder owning at least 25% of the shareholding. In other cases, the ordinary treatment for dividend distributions from Norwegian companies applies. The non-treaty rate is 25%. A dividend distribution to corporate shareholders resident in EEA countries is normally exempt from withholding taxes (regardless of tax treaty provisions).

In the event that a company with a corporate shareholder owning at least 25% has a mixture of upstream petroleum activities and other activities, withholding tax on dividend distributions (within the limitations given in a tax treaty/ distributions to EEA corporate shareholders) would be applied on an apportioned basis to the non-upstream component.

6.2 Interest

There are no withholding taxes on interest and royalty payments according to Norwegian tax law.

6.3 Other

Not applicable. It should be noted Norway does not have the concept of branch profits remittance tax or the like.

6.4 Tax treaties

Norway has entered into a large number of income tax treaties with other countries, potentially allowing for reduced withholding tax on dividend distributions (compared to the non-treaty rate of 25%).

7.0 Indirect taxes

7.1 Value added tax, goods and services tax and sales and use tax

Norway operates a traditional VAT system. The sales of goods and services are normally subject to VAT at a rate of 25%.

However, goods and services supplied outside a 12 nautical mile zone of the Norwegian mainland are not subject to VAT.

Moreover, the supply of goods and services outside the 12 nautical mile zone in connection with the exploration and production activities on the NCS are normally zero rated.

Sale of crude oil and gas made by licensees will in practice always be zero rated (sales within Norway are subject to the ordinary rate of 25%).

Import of goods into Norway's customs zone are generally subject to import VAT. The customs zone consists of the mainland and 12 nautical miles outside the mainland. Therefore goods that are provided to e.g. installations outside the Norwegian customs zone are not subject to the import VAT.

If goods are placed in a customs warehouse, in transit or temporarily imported into Norway, import VAT may also be avoided.

7.2 Area fee

The area fee contributes to efficient exploration of the assigned area in order for the resources to come into production as soon as possible in addition to ensuring a long production time for existing oil fields. As rule, the area fee is not payable for areas in production or with adequate exploration activity.

All production licences are exempt from the area fee during the initial licence period. The initial production period can last up to ten years, but is normally set to between four and six years. Accordingly, the area fee normally starts to apply from years five to seven after the initial licence was awarded.

After a PDO has been filed with the Ministry of Oil and Energy, area fees are not payable for the area limiting the deposits included in the PDO. These areas are exempt from the area fee from the date of the PDO and until the last day of production. After the production has ceased, the area fee will usually be escalated over three years at the rates mentioned below.

The fee may also be reduced or abolished in other cases. If the licensee, after the initial licence period, drills an exploration well, they may upon application be exempt from the area fee for the relevant field for two years.

The annual area fee for most licences increases from Norwegian Kroner ("NOK") 34,000 per square kilometre the first year the fee is payable, to NOK 68,000 per square kilometre the next year up to the maximum of NOK 137,000 per square kilometre the subsequent years.

The area fee is payable in advance for each calendar year to the Oil Directorate. Payments are normally made by the operator.

7.3 Customs duties

Customs duties in Norway are mainly limited to food and clothes in Norway. Customs duties on such items may also be avoided to the same extent as import VAT may be avoided. See Section 7.1 above for further information.

7.4 Environment taxes

Carbon dioxide tax

Carbon dioxide tax is levied at a rate per square cubic metre ("scm") of gas burnt or directly released and per litre of petroleum burnt. The rate for 2014 is NOK 0.98 per litre of petroleum or 0.98 per scm of gas.

All participants in a production licence are jointly responsible for the carbon dioxide tax and payments must be made to the Oil Directorate. The carbon dioxide tax for the period January to June should be paid by 1 October and the carbon dioxide tax for the period July to December should be paid by 1 April the following year. Documentation for the amounts of burnt or released gas or petroleum must be sent to the Oil Directorate twice a year.

These obligations are typically handled by the operator of the oil field.

Moreover, carbon dioxide tax is levied on import of certain mineral products for 2014 are; e.g. natural gas: NOK 0,66 per scm, LPG: NOK 0,99 per kilogram

Nitrogen Oxide Tax

The rate of nitrogen oxide tax for 2014 is NOK 17,33 per kilogram waste of nitro oxide from flame stacks on offshore and onshore installations. Payments are usually handled by the operator.

7.5 Stamp tax

Stamp taxes are not levied on transfers other than those of real property in Norway.

8.0 Other

8.1 Choice of business entity

It should be noted that production licences as a starting point only are granted to Norwegian companies. Companies resident in another EEA country may also qualify.

Pass through agreements may allow a non-Norwegian group company to perform the activities on behalf of the Norwegian licensee, which implies that the non-Norwegian company is taxed according to the rules described elsewhere in this chapter on Norway. Withholding taxes are never levied on distribution of branch profits.

Companies having sharing production licences enter into joint operating agreements which in effect imply that there is a partnership between the licensees. The parties are joint and severally responsible towards the authorities for its obligations according to the Law on Petroleum Activities and to a great extent also towards third parties. The partnership is not a taxable entity and there is no co-ordination between the tax positions pertaining to each partner.

8.2 Foreign currency

Norway does not have any exchange control rules affecting corporations. Statutory accounts will generally be worked out in NOK. However, enterprises that mainly have transactions in another currency may use this currency in their statutory accounting. However, taxes are calculated in NOK regardless of whether their statutory accounts prepared in NOK.

9.0 Oil and gas contact information

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