HMRC - OT05362 - PRT: Valuation Of Non-Arms Gas - Valuation Of Light Gases To 31 December 1993

OTA 1975 made no special provision for the valuation of gas and the basic rule designed for oil (monthly values) applied. At the time however the point was not material as most of the gas produced was sold to British Gas Corporation and there were few non-arms length disposals to value.

The issue first became important in connection with ethane used for petrochemical purposes and this led to the election legislation in FA82\S134 and FA82\SCH18. Under these provisions a participator could elect for ethane used for such purposes to be valued on a long term basis by reference to a formula he proposed instead of being valued on a short term basis under OTA75\SCH3\PARA2. Under the election the participator identified the gas covered, the period of the election (which could be up to 15 years) and the formula (usually a base price plus escalator) to be used to establish the market values. The Board accepted the election if it was satisfied that the formula proposed gave values which were, over the period of the election, not materially different from the prices which would have been obtained in an arm’s length contract for the sale of the ethane in question. The ethane was then valued accordingly and companies obtained the certainty that was absent in the monthly valuation methodology.

The legislation was challenged in a judicial review brought by ICI (Regina v Attorney General ex parte Imperial Chemical Industries Plc 60TC1, [1987]1CMLR72). The points made by the Court of Appeal which may still be relevant are covered in OT05430.

The legislation was extended to cover all light gases by FA86\S109 and SCH21. Considerable adaptation and extension of the rules for ethane were required to make them suitable for the valuation of gas meeting the specification for entry into the national transmission system (grid spec. gas); particularly to introduce provisions for take or pay and capacity payments. The resulting legislation was rather complex and prescriptive. It proved to be unwieldy and occasionally anomalous in valuing the increasing number and variety of non- arm’s length disposals which followed the opening up to competition of the gas market initiated by the Monopolies and Merger Commission report of 1988. FA94\S236 and SCH23 abolished the election legislation and took light gases out of the monthly valuation rule with effect from 1 January 1994. A new rule was introduced into OTA75\SCH3\PARA3A (see OT05375). Any election made on or before 31 December 1993 continues in force until expiry subject to the provisions for re-opening.

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