HMRC - OT09050 - Expenditure - Searching

OTA75\S3(1)(a)

For expenditure to be allowable under OTA75\S3(1)(a) it must be incurred on searching for oil within the field as determined by the Secretary of State, or within a distance of 5 kilometres (km) of the field PRT boundary. Such exploration costs will normally include preliminary geological field studies, seismic surveys and their interpretation, and the drilling of exploration wells and their evaluation. The bulk of this expenditure will generally have been incurred before the determination of the field. The view that entitlement to relief under Section 3(1)(a) does not come to an end with field discovery was endorsed by CIR v Amerada Hess (TL 3632).

Significance of the 5km boundary

The case of CIR v Amerada Hess Ltd also made it clear that all expenditure on searching for oil within 5 km of the field boundary qualifies for relief under that subsection whether or not the activity is targeted at the field, and irrespective of whether it is successful. The test is a geographic one in relation to the field. The decision went against LB Oil & Gas’s previously held view that for a claim to be allowable the claimant needed to show that the purpose of the expenditure related to the field of claim, e.g. extending an existing field.

In such cases, care should nonetheless be taken to test that non field-specific expenditure within the 5 km is allowable on this geographic basis. Appraisal drilling, for example, is unlikely to qualify as the expenditure will be allowable under OTA75\S3(1)(c) (see OT09100), which has no 5 km test. Likewise, in a safeguard period, searching costs of this kind may fall foul of the rules in OTA75\S9A (see OT17500) as they will not constitute ‘capital expenditure’ for the purposes of that section.

Expenditure on searching for oil outside the 5 km boundary, which is expected to extend the field, will not qualify for relief unless it results in a re-determination of the field. As a re- determination is a determination the expenditure will have been incurred in ‘searching for oil anywhere within the area of the field as subsequently determined’.

For items such as seismic expenditure, where the work is partly within and partly outside the qualifying area, an apportionment is usually made on the basis of km shot or some other suitable basis. For apportionment of operating expenditure generally, see OT09375.

Exploration and appraisal relief

From 16 March 1983 until 15 March 1993 inclusive, expenditure incurred on exploration and appraisal (E&A) could be considered for relief under OTA75\S3(1)(a) or OTA75\S5A, see also OT13975. E&A expenditure incurred after 15 March 1993 (subject to a limited extension under transitional provisions, see OT14040) is now only relievable under OTA75\S3(1)(a) (in the case of exploration or searching) and under OTA75\S3(1)(c) (in the case of appraisal or ascertaining, see OT09100.

‘Exempt gas’ fields

There are special rules in OTA75\S10(3A)-(3C) relating to expenditure otherwise allowable under OTA75\S3(1)(a) where the oil won from a field (or expected to be won) includes ‘exempt gas’, see OT13240.

Farm-in Agreements

OTA75\S3(1)(a) also covers work undertaken by means of a farm-in agreement and such costs may include bottom hole contributions, (see OT13875) to works undertaken by others in the relevant area. Reimbursement of prior costs incurred by the farmer-out are not included although those costs may still qualify in their own right for inclusion in a Schedule 5 field claim made by the Responsible Person.

Previous page

Next page