HMRC - OT09300 - Expenditure - Redundancy

Redundancy payments commonly include both a statutory and a non-statutory element. OTA75\S3(2) governs the allowance of statutory redundancy. Non-statutory payments may be allowable under OTA75\S3(1)(d), to the extent they are a cost of ‘winning oil’ (see OT09125), though they may also qualify under other parts of OTA75\S3(1).

Statutory redundancy, OTA75\S3(2)

The statutory element is allowable for PRT under OTA75\S3(2), and may be claimed in any field.

The costs allowable under OTA75\S3(2) are defined by reference to ICTA88\S579 and ICTA88\S580. Here the term ‘redundancy payment’ is given the same meaning it has in the Employment Protection (Consolidation) Act 1978 (or, if appropriate, Part III of the Contracts of Employment and Redundancy Payments Act (Northern Ireland) 1965).

The test for OTA75\S3(2) relief is whether the payment is allowed under ICTA88\S579 for the company’s ring fence trade. But the provisions differ in that ICTA88\S579 requires any rebate to be treated as a receipt of that trade, whereas, for PRT, the rebate reduces the allowable amount of the redundancy payment.

Additional amounts may be allowable against ring fence profits in respect of payments under oil industry agreed schemes, or under ICTA88\S90, but such payments are not allowable for PRT.

In some cases there will be an agreement, often in the Joint Operating Agreement, that part of an operator’s redundancy payments will be met by partners in the field or exploration joint venture. These payments will be allowable for PRT in the partners’ hands on the same basis as if they had been claimed by the operator, i.e. the statutory element only will be within OTA75\S3(2). It is usually necessary to obtain details of the statutory\non-statutory split from the operator.

Non-statutory redundancy

Non-statutory redundancy costs are allowable in the field to which they relate under OTA75\S3(1)(d) as ‘winning’, provided it can be shown that the costs were incurred for the purpose of improving the relevant field’s production efficiency or prolonging its life and the like. In contrast, costs incurred as part of a corporate restructuring or disposal of a field interest are not allowable.

Nor in the view of LB Oil & Gas will redundancy costs incurred as a consequence of closing down a field or an asset be allowable since this expenditure is not incurred for the purpose set out in OTA75\S3(1)(i), see also OT10050.

It is not possible to produce an exhaustive list of the circumstances in which non-statutory redundancy costs will be allowable, as each case must be decided in the light of its particular facts, but the following redundancy costs are very unlikely to be allowable:

those incurred on a sale of a field interest

those incurred on the abandonment of a field

those incurred generally on cessation of a trade

those incurred for staff of a general overhead nature

those relating to relocation costs

those stemming from general corporate downsizing.

On the other hand, redundancy costs incurred

as a result of the acquisition of a field interest and

as a result of taking over the operatorship of a field

will be allowable if it can be shown that the purpose of the redundancies was to reduce costs in order to carry on the winning of oil by maintaining or extending field life. If, however, those costs are incurred by the vendor or old operator, they are unlikely to qualify as the purpose will generally be related to the disposal of the old interest or operatorship.

Cost-cutting which will result in more profit will not always qualify as winning etc. Where redundancy costs are incurred to reduce the cost structure of a field, in order to maintain its life, this clearly appears to be winning. But LB Oil & Gas does not accept that the reduction of costs resulting from a general corporate initiative following a merger or general corporate downsizing will qualify for PRT relief.

Redundancy costs met by fellow participators

Where fellow participators have agreed to share some of the Responsible Person’s (RP) redundancy costs, this is likely to be a factor in suggesting that expenditure relates to the field. However, the interests and concerns of the participators may be sufficiently close to make joint contributions to various initiatives a cost-effective proposition, even though they do not relate directly to an allowable field purpose and are not therefore allowable. Once again it will be critical to examine all the facts.

Accounting treatment

The accounting treatment of the expenditure may be indicative of its purpose, e.g. exceptional merger costs may be treated separately from other cost reduction initiatives, both in the accounts and in the management information.

Previous page

Next page