HMRC - OT20405 - EU Emissions Trading Scheme - Phase I

The following treatment has been agreed with UKOITC.

CT and supplementary charge:

Costs associated with the purchase or trading of EU ETS allowances in connection with the requirement to meet emissions requirements of ring fence installations are deductible as costs of the ring fence trade.

Income associated with the sale of EU ETS allowances allocated to installations within the ring fence is taxable within the ring fence.

PRT

Costs associated with the purchases or trading of EU ETS allowances to meet any annual shortfall of allowances are deductible as a cost of winning oil under section 3(1)(d) OTA 1975.

Income arising from any disposals associated with the sale of surplus EU ETS allowances is not subject to PRT.

Penalties

The tax treatment of penalties has not been agreed with UKOITC. LB Oil and Gas continues to take the view, and this is held more widely within HMRC, that the EU ETS penalty is punitive in nature and is not compensatory or part of a contractual arrangement.

The non-deductibility of such penalties for tax purposes is an established UK case law principle. It should be treated as a fine that is incurred as a result of the infraction of the law and is not incurred wholly and exclusively for the purposes of the ring fence trade or as an allowable cost for PRT.

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