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NOTE OF A MEETING HELD IN NUMBER 11 DOWNING STREET AT  
5.30 P.M. ON THURSDAY 5 FEBRUARY, 1981.

PRESENT:

Chancellor of the Exchequer (in the chair)

Chief Secretary	Mr Dalton	) Inland
Financial Secretary	Mr Pollard	) Revenue
Minister of State (Commons)		
Mr Ryrie		
Mr Middleton		
Mr Battishill		
Mr Wicks		
Mr Sedgwick		
Mr Corlett		
Mr Tyler		
Mr Tolkien		

Mr Cropper

NORTH SEA FISCAL REGIME

The Chancellor invited the meeting to consider the issues as they were set out in Mr Corlett's agenda of 4 February.

Supplementary Petroleum Duty (SPD)

2. The Chancellor noted that the oil companies had not appeared to dispute that extra taxable capacity existed for 1981-82. In general they had concentrated on attacking the form of the new tax - some said they would prefer a temporary levy, others some form of advancement of PRT. He believed it would be difficult to fix the rate of the new tax at more than 20 per cent in the light of the indication of rate he had given in this Statement of 24 November, and the fact that he also wanted to do something on smoothing of North Sea taxation receipts.

3. He himself was convinced that the form of the new tax was the right one, but he was attracted to the idea of having it formally renewable next year. This would be a useful presentational concession to the oil companies, and would give them a further opportunity to develop their ideas for a better tax and submit them to the Government. The Financial Secretary said that he would accept this, provided the Government could claim credit for the projected revenue from the new tax in the medium term financial strategy.

#### The US dimension

4. Mr Dalton said that some US companies had expressed concern about problems of creditability of the UK North Sea taxes. The companies were aware that it was most unlikely that the SPD would be accepted by the US Internal Revenue Service as a creditable deduction against US taxation. The new tax would lessen the amount of PRT paid by many US companies, and hence lower the amount of overseas tax which they could credit against their US tax liability. They were therefore seeking to be allowed to spread their PRT liabilities. Since the cost of this would fall on the US Treasury this was a concession which might well be made. The difficulty was that it was unlikely that US Treasury officials would be willing to see UK officials to discuss this in time for the Budget. The Chancellor said

that it should be assumed that he would announce in his Budget that he was ready to consider spreading PRT payments and do it retrospectively to 1 January 1981, depending on the outcome of consultations with the US Treasury. On this issue, as on PRT uplift, it was necessary to be careful that changes to PRT did not destroy its status as creditable under the US/UK Double Taxation Treaty. Mr Dalton said that Esso claimed to have a particular problem. Despite US tax pooling arrangements it did not have enough world-wide overseas tax with which to offset the reduction in PRT liability which would result from the introduction of the new tax. The Revenue had asked to see Esso figures on their world-wide tax position. However, in the final analysis, the UK tax system could not necessarily be tailored to suit Esso's particular problems.

#### Petroleum Revenue Tax

5. It was agreed that safeguard should be retained, but only to run for a limited period in the life of each field. A final decision on the length of the period would need to be made once it was known what changes could be made to uplift.
6. It was agreed that no change should be made in the oil allowance.
7. The Chancellor said that officials were recommending that uplift should be cut off four years after a field comes on stream, or after pay back if companies could suggest a water-tight definition. Mr Sedgwick said that this was the heart of

the "wasteful expenditure" problem, and it had to be tackled if future North Sea revenues were to be protected. Mr Dalton said that the problem was that it would be hard to get a definite view out of the IRS as to whether the changes contemplated would lead US officials to change their view on whether PRT should continue to be creditable under the UK/US Double Taxation Treaty. It was agreed that Mr Pollard would seek an early meeting with the IRS in Washington in the week beginning 9 February to sound out their informal views. The Chancellor agreed to the MST(C)'s suggestion that the Inland Revenue should produce a note on the cost of one year's delay in making the proposed changes to uplift.

#### Smoothing

8. The Chancellor believed that either SPD or PRT should be smoothed. The MST(C) said that he would like to take this opportunity to simplify the North Sea regime by phasing out Advance PRT. The Financial Secretary accepted that simplification was desirable, but <sup>said</sup> he would prefer to see the legal mechanism for advancement retained for the time being in case it was needed later. The Chancellor said that in order to be sure of smoothing at least one of the taxes he might announce in the Budget that he also wished to smooth PRT payments. If, as seemed likely, this created an outcry he might withdraw this as a concession, on the understanding that the new tax was smoothed.

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9. The Chancellor said that he would want to inform Mr Howell of his decisions next week, but he would not do so before Mr Pollard had sought to obtain from the IRS an informal view on the creditability of PRT with <sup>the</sup> changes that were being proposed on uplift.

A. TYLER

9 February 1981

Distribution

Those present

Sir D Wass

Mr Unwin

Mr Thornton

Mr. Ridley

Mr. Cardona

PS/Inland Revenue