

Neutrality and Efficiency of Petroleum Revenue Tax: A Theoretical Assessment

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Abstract

We use an irreversible investment model of oil development to show how a fiscal regime can be both neutral with respect to development decisions and efficient in recouping economic rents. We find that there is a unique rate for calculating the tax deductibility of capital costs which ensures economic neutrality; while tax efficiency involves high rates of tax on profits after these deductions. Using parameters of the UK Petroleum Revenue Tax (PRT), numerical calculations in our simplified model suggest that PRT was both neutral and relatively efficient. In conclusion the tax efficiency of PRT is compared with that of a neutral resource rent tax.

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