Who owns the barrel: service fees for North Sea extraction

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ENERGY PAPER 01

Who owns the barrel: service fees for North Sea extraction

The state already owns the oil. It should pay a contractor to lift the barrel and keep it, instead of handing the barrel over and taxing the profit.

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> THE ASK
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> That the statutory terms for any future North Sea licensing round vest ownership of the extracted oil and gas in the state, with operators paid a contracted service fee.

The United Kingdom is unusually exposed to fossil fuel price shocks, and the exposure is structural. When the Organisation for Economic Co-operation and Development (OECD) assessed the economic damage of the Iran conflict in Mar 2026, it found the UK had taken the largest growth downgrade of any Group of Twenty (G20) member, half a percentage point off an already weak forecast, alongside the sharpest upward inflation revision of any major advanced economy.[1] The OECD gave a one-line explanation. The UK imports most of its oil and gas and holds very little in storage, so it should cut the dependence.

The debate that followed has been an argument about amounts, covering how much to tax North Sea profits, how many licences to grant and how long a windfall levy should last. Nobody has questioned the arrangement underneath the amounts. The state owns the barrel until the moment it surfaces, gives it away at the wellhead, and then negotiates for a share of the proceeds through the tax system. That is where the money leaks.

Who owns the barrel at the wellhead

Petroleum in the ground already belongs to the state. The Petroleum Act vests ownership of the resource in the Crown, and has since 1934.[2] A licence, once granted, transfers ownership of what is extracted to the operator, and the public interest in the resource is then pursued by taxing the operator's profits afterwards, through instruments that change with each fiscal event. The Energy Profits Levy, layered on top of the permanent regime in 2022, has been amended repeatedly since.[3] Operators price that instability in. The country loses revenue it should have collected, and investment it never sees.

Nothing requires this arrangement. It is one design among several, and other producing nations chose differently.

The proposal

Any future extraction licence should vest ownership of the extracted oil and gas in the state, with the operator paid a contracted fee for the work of lifting it.

The operator's return becomes a margin on a service instead of a share of a commodity, and the commodity stays with the state, to sell, store or allocate as policy requires. Three things follow.

Economic rent from a national resource flows to the public, rather than to shareholders, many of whom are not resident UK taxpayers.

The state can hold a strategic reserve acquired at the cost of extraction rather than at market price, a direct tool against exactly the shocks the OECD warns of.

The state can offer discounted energy to households and industry as deliberate policy, rather than depending on subsidy schemes that chase market prices after the fact.

Existing licences are untouched; the model binds new licences only, which is how Brazil introduced production sharing for its pre-salt fields in 2010, leaving existing concessions in place.[4] In a period when few new licences are being granted, the change costs nothing now. It sets the statutory terms that apply whenever licensing resumes, and settling those terms in advance is cheapest precisely because no revenue is at stake yet.

What Iraq already pays the majors to do

Norway retains direct state ownership of a substantial share of production through the State's Direct Financial Interest, and the returns compound in the Government Pension Fund Global, now the largest sovereign wealth fund in the world.[5] The cleanest service-fee precedent is Iraq, whose post-2009 technical service contracts pay international operators a fixed remuneration fee per barrel while the state keeps the oil.[6] Companies including BP, Shell, ExxonMobil and TotalEnergies signed those contracts and operated under them for years. The claim that major operators will not work for a fee is contradicted by the fact that they do.

Why a tax cannot hold a reserve

The standard answer to resource rent is the tax system, and the UK already has a windfall instrument. A tax cannot deliver the reserve or the discount. A levy captures a share of the operator's profit after the commodity has been sold at market price; it cannot put a single barrel in storage at cost, and it cannot supply a hospital or a steelworks below market price during a shock. Ownership can do both. Predictability also runs in the state's favour, since a contracted fee makes public revenues a function of volume rather than price, which a spending review can actually plan on.

The proposal has an honest cost, and it is price risk. Under a service fee the state, not the operator, holds exposure to the commodity price. When prices crash the state's barrels are worth less while the fee is still owed, so fees must be set to keep marginal fields viable across the cycle, and the contracts must say in advance how fees adjust. Iraq's experience carries the warning as well as the precedent, because fee levels set too rigidly strained operators and state alike when prices moved.[6:1] That is a hard piece of contract design, and every producing nation that chose ownership has done it.

The filter

The change also does something to the argument itself. This is about incentives, not motives. Under the current arrangement, advocacy for new drilling is inseparable from advocacy for private commercial upside, and a reader cannot tell which is being argued for. Under a service-fee regime the two come apart, and advocacy for drilling becomes advocacy for the public balance sheet, and nothing else. Anyone whose stated case for the North Sea is jobs, energy security and the national interest loses nothing under these terms, because the fee pays for the jobs and the state banks the security. Objection to those terms therefore tells you something.

Objections

Operators will not accept it. The rigs, the infrastructure and the expertise are already in the basin, and a service fee pays a return on all of it. What it removes is uncapped commodity upside. Sovereign owners from Norway to Iraq have set such terms and found international majors willing to sign.[6:2]

It is anti-extraction. The opposite is true. Oil and gas will be needed for decades, and the pragmatic position is to extract on terms that build public wealth rather than leave the value offshore. A government confident in these terms can grant licences more freely, not less.

It disrupts investment. A firm that dislikes the terms is free not to bid, the terms are common practice internationally, and capital has not fled the countries that use them.

There is nothing to license. Then the legislation is free. The next round, whenever policy or circumstance produces one, happens on the public's terms by default rather than after a rushed argument.

SOURCES

1. OECD, interim Economic Outlook, 26 Mar 2026. UK growth downgraded 0.5 percentage points to 0.7% for 2026; CPI forecast raised to 4%. ↩
2. Petroleum Act 1998, s.2, consolidating Crown ownership of petroleum first vested by the Petroleum (Production) Act 1934. ↩
3. Energy (Oil and Gas) Profits Levy Act 2022, as subsequently amended. ↩
4. Law No. 12,351/2010 (Brazil), establishing production sharing for pre-salt areas; pre-existing concessions were not converted. ↩
5. Norwegian Ministry of Energy, the State's Direct Financial Interest (SDFI), managed through Petoro; returns transfer to the Government Pension Fund Global. ↩
6. Iraq Ministry of Oil, technical service contracts awarded in the 2009 licensing rounds; fixed per-barrel remuneration fees paid to contractors including BP, Shell, ExxonMobil and TotalEnergies, with subsequent renegotiation of fee terms. ↩ ↩ ↩