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PAYING FOR THE "NO"?
NORWEGIAN PETROLEUM AND THE EUROPEAN UNION

In the referendum of November 28, 1994, Norway voted "no" to membership in the European Union (EU). Parts of the petroleum industry may have been indifferent to this vote. However, the lack of influence on the determination of the Union's excise taxes on petroleum, and, possibly, on the processes towards more liberal gas markets, as well, may prove to incur a cost to the country in the future.

Norway is producing oil and natural gas at a record pace. In 1994, she reached a level of 2.6 million barrels of oil per day (mb/d), and 27 million cubic meters (BCM) of gas for a total of some 140 million tons of oil equivalent (mtoe), an all-time record. Production is expected to increase further, with oil production passing 3 mb/d and gas production reaching 50-60 BCM/year within few years, a total of some 200 mtoe. The great hydro power production and its export potential only reinforces the picture of a dominant energy exporting country in Europe, and one of the largest in the world. The role as an "energy superpower" is a challenge for Norway, being a country with only 4.5 million inhabitants. Energy may attract more EU and world attention to Norway than any other issue, perhaps besides military security. The EU buys all Norwegian gas and most of her oil.

In the Norwegian economy, the petroleum sector is playing a significant role, too. Today, it accounts for about 15 per cent of Gross National Product and one-third of total export revenues. Its share of the economy is expected to rise due to increase in production, and possibly oil prices. In addition, the offshore supplies industry plays an important economic, political, cultural, and social role in Norway's regions.

Since the start-up of production in the 1970s, Norwegian international energy policy has balanced various interests within the country, for example of regional kind, against interests from abroad, such as those emanating from OPEC, the IEA, and others. As EU energy, environmental and fiscal policies gradually become harmonized across member states, the Community is, eventually, becoming an additional actor on Europe's energy scene, probably the most important one.

One central aspect of the establishment of EU's Single market (SIM) is to increase competition across industries. Norway participates in SIM through the European Economic Area

(EEA) agreement. Thus, in spite of the "no" vote, Norway already practices international competition in the allocation of contracts to the offshore supplies industry. The rights to develop oil and gas fields are allocated on a non-discriminatory basis, as well. Downstream, Norwegian companies may increase activities in markets and integrate vertically and horizontally, to the same extent as if she had voted a "yes". A difference to a membership is, however, that as a non-member, Norway has no right to vote over competition rules.

The membership question becomes more complex when prices of crude oil and natural gas are concerned. The prices that Norway as a producer receives, are in part determined by policy-dependent factors such as the use of excise taxes and the processes towards more liberal gas (and electricity) markets.

Over the previous 20 years, taxes on oil products have become increasingly more popular among consuming countries. Often environmental protection costs are cited as reasons for raising taxes. Irrespective of the credibility of the argument behind their existence, orchestrated excise taxes across petroleum consuming countries push consumers' prices up and producers' prices down. As only few countries are producers, such as Norway, and EU countries mostly are consumers, the downward pressure on producers' prices represents huge transfers of rent from producers (and consumers) to consuming countries' treasuries.

In Europe today, taxes as percentage share of consumer prices on gasoline, range between 70 and 80 per cent. While producers receive some 17 $/bbl for crude oil, consumers pay some 80 $/bbl. The difference is made up by taxes. In the early 1980s, when the price of oil was 35 $/bbl, consumers paid about 60 $/bbl. The low oil prices of the 1990s are partly resulting from massive increases in petroleum taxation of consumers, particularly over the last 10 years.

Excise taxes on gas are used to a much lesser degree than on oil. If, however, gas taxes should be increased and end-users' prices continue to be linked to prices of its alternatives, such as fuel oils, a gas tax will largely be paid by producers.

For Norway, worst case scenario occurs if excise taxes on gas are raised at the point in time when fields and pipelines on the NCS are "fully" developed. In such a situation, most producers' costs are sunk, and there is no alternative but to continue supplying through existing facilities and grids even if prices are well below what was expected. In the extreme, if no new production capacity is available or planned for, taxes could be raised to the point where producers' prices are pushed down to a level that covers just a little more than variable costs. In fact, with all cost sunk, producers would benefit from continuing production, even with a loss.

In addition to the tax issues, the development of new market structures, competition rules, regulation and other aspects of the processes towards more liberal European energy markets, in particular for natural gas, may affect producers' prices, as well. Even marginal changes in contractual and market terms constitute huge amounts of money for all parties involved.

The non-member status makes Norwegian influence weaker both in the determination of excise taxes and in the formulation of new market structures. The possibility of becoming a preferred supplier of gas in relation to non-European gas or polluting coal deteriorates, as well. It may become more difficult to achieve goals through lobbyists, several bilateral contacts, political rhetoric, alliances through companies inside the EU, contacts with other gas producers etc., than through a membership. When strong interest conflicts appear, the exporting outside-country's interests may well be disregarded. On the other hand, as part of the process towards a more liberal gas market, it will probably be more difficult for the EU to introduce competition across gas sellers (abolishment of the Gas Negotiation Committee, GFU) on the NCS when Norway remained on the outside.

The huge flow of petroleum from Norway to the EU has shaped an interdependence between the two, irrespective of the membership question. As the "energy superpower" of Western Europe, Norway must be aware that none of her friends and allies within the Union share her interests in the distribution of rent. A strengthening of Norwegian policies to take care of her specific interests as petroleum exporter may prove necessary to compensate for potential losses caused by the lack of formal influence on the European Union's policies.